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HOUSE OF COMMONS

First Session—Twenty-seventh Parliament

1966 - 67

STANDING COMMITTEE

ON

FINANCE, TRADE AND ECONOMIC AFFAIRS

Chairman: Mr. HERB GRAY

MINUTES OF PROCEEDINGS AND EVIDENCE

No. 22 - 34

TUESDAY, NOVEMBER 8, 1966

Respecting

Bill C-190, An Act to amend the Bank of Canada Act.

Bill C-222, An Act respecting Banks and Banking.

Bill C-223, An Act respecting Savings Banks in the Province of Quebec.

WITNESSES:

Messrs. S. T. Paton, President, *The Canadian Bankers' Association*; Leo Lavoie, Vice-President, *The Canadian Bankers' Association*; J. H. Coleman, Vice-President, *The Canadian Bankers' Association*; W. T. G. Hackett, Chairman, *Canadian Bankers' Association Bank Act Revision Committee*; R. M. MacIntosh, Joint General Manager, Bank of Nova Scotia; Mr. C. F. Elderkin, Inspector General of Banks.

ROGER DUHAMEL, F.R.S.C.

QUEEN'S PRINTER AND CONTROLLER OF STATIONERY  
OTTAWA, 1966

HOUSE OF COMMONS  
First Session—Twenty-seventh Parliament  
1968

STANDING COMMITTEE  
ON  
FINANCE, TRADE AND ECONOMIC AFFAIRS

Chairman: Mr. Herb Gray

Vice-Chairman: Mr. Ovide Laflamme  
and Messrs.

Addison,	Comtois,	Leboe,
Basford,	Flemming,	Lind,
Cameron ( <i>Nanaimo- Cowichan-The Islands</i> ),	Fulton,	McLean ( <i>Charlotte</i> ),
Cashin,	Gilbert,	Monteith,
Chrétien,	Irvine,	More ( <i>Regina City</i> ),
Clermont,	Lambert,	Munro,
Coates,	Lamontagne,	Valade,
	Langlois ( <i>Mégantic</i> ),	Wahn—(25).

Dorothy F. Ballantine,  
Clerk of the Committee.





## MINUTES OF PROCEEDINGS

TUESDAY, November 8, 1966.

(38)

The Standing Committee on Finance, Trade and Economic Affairs met at 11:05 a.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Addison, Cameron (*Nanaimo-Cowichan-The Islands*), Cashin, Chrétien, Clermont, Comtois, Flemming, Fulton, Gilbert, Gray, Laflamme, Lambert, Leboe, Lind, McLean (*Charlotte*), Monteith, More (*Regina City*) (17).

*Also present:* Messrs. Grégoire and Laprise.

*In attendance:* Messrs. S. T. Paton, President, The Canadian Bankers' Association and Vice-President and Chief General Manager, The Toronto-Dominion Bank; Leo Lavoie, Vice-President, The Canadian Bankers' Association and Vice President and General Manager, La Banque Provinciale du Canada; J. H. Coleman, Vice-President, The Canadian Bankers' Association and Chief General Manager, The Royal Bank of Canada; W. T. G. Hackett, General Manager (Investments), Bank of Montreal and Chairman of Canadian Bankers' Association Bank Act Revision Committee; Gilles Mercure, Assistant General Manager, La Banque Provinciale du Canada; F. L. Rogers, Economic Adviser, The Bank of Nova Scotia and Chairman, Canadian Bankers' Association Economists Committee; R. M. MacIntosh, Joint General Manager, Bank of Nova Scotia; J. H. Perry, Executive Director, The Canadian Bankers' Association; and C. F. Elderkin, Inspector General of Banks.

On motion of Mr. Clermont, seconded by Mr. Leboe,

*Resolved*,—That the amendments to Bills C-222 and C-223 tabled by the Inspector General of Banks at the afternoon sitting on Thursday, November 3, 1966, be appendices to the Minutes of Proceedings and Evidence of that date. (*See Appendices H and I, Issue No. 21*).

On motion of Mr. Laflamme, seconded by Mr. Gilbert,

*Resolved*,—That the evidence taken at the afternoon sitting on Thursday, November 3, 1966, be part of the official Proceedings. (*See Issue No. 21*).

The Committee resumed consideration of the banking legislation.

The Chairman introduced the President of the Canadian Bankers' Association, Mr. Paton, who in turn introduced the others in attendance.

At the invitation of the Chairman, Mr. Paton summarized the brief submitted by the Canadian Bankers' Association, copies of which had previously been distributed to the members. (In accordance with the resolution passed at the meeting of October 13, 1966, the brief is attached as *Appendix J*).

At the request of the Chairman, Mr. Paton also explained the role of the Canadian Bankers' Association and tabled copies of his statement, which were distributed to the members.

Mr. Paton and Mr. Lavoie were questioned.

The questioning continuing, at 12:50 p.m., the Committee adjourned until 3:45 p.m.

#### AFTERNOON SITTING (39)

The Committee resumed at 3.55 p.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Addison, Cameron (*Nanaimo-Cowichan-The Islands*), Clermont, Comtois, Flemming, Fulton, Gilbert, Gray, Laflamme, Lambert, Leboe, Lind, McLean (*Charlotte*), Monteith, More (*Regina City*), Wahn—(16).

*Also present:* Messrs. Caouette, Grégoire and Latulippe.

*In attendance:* The same as at the morning sitting.

Mr. Elderkin tabled three exhibits, as follows, copies of which were distributed to members:

*Exhibit No. 15:* Trust Companies in Canada having Directors who are also Directors of Chartered Banks at March 1, 1966.

*Exhibit No. 16:* Insurance Companies in Canada having Directors who are also Directors of Chartered Banks at March 1, 1966.

*Exhibit No. 17:* Loan Companies in Canada having Directors who are also Directors of Chartered Banks at March 1, 1966.

Questioning of the witnesses was resumed, and Messrs. Paton, Coleman, Hackett and MacIntosh were questioned.

At 4:30 p.m. the Vice-Chairman, Mr. Laflamme, took the Chair and at 4:50 p.m. the Chairman resumed the Chair.

During the questioning, Mr. Grégoire read into the record extracts from correspondence between himself, the Bank of Canada, the chartered banks and the Minister of Finance, as well as from a publication of the Royal Bank of Canada entitled *Economic Trends and Topics*.

In reply to a question, the witness tabled a paper entitled *Cash Ratio Management—Proposed "Twice-Monthly" Averaging Technique*, copies of which were distributed to the members.

The questioning continuing, at 5:55 p.m., the Committee adjourned until 8:00 p.m. this day.



EVENING SITTING  
(40)

The Committee resumed at 8:10 p.m., the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Addison, Cameron (*Nanaimo-Cowichan-The Islands*), Clermont, Comtois, Fulton, Gilbert, Gray, Laflamme, Lambert, Leboe, Lind, McLean (*Charlotte*), Monteith, More (*Regina City*), Wahn—(15).

*Also present:* Messrs. Caouette, Grégoire, Latulippe, Pilon and Saltsman.

*In attendance:* The same as at the morning and afternoon sittings and Mr. L. Hebert, Deputy Governor, Bank of Canada.

Mr. Clermont moved, seconded by Mr. Leboe, that copies of the correspondence read into the record by Mr. Grégoire and the pamphlet of the Royal Bank be distributed to members and attached as an appendix to this day's Minutes of Proceedings and Evidence. Mr. Grégoire tabled the documents in question.

The representatives of the chartered banks, of the Minister of Finance and the Bank of Canada present having consented to the documents being distributed and printed as an appendix, the motion was carried. (*See Appendix K*).

On motion of Mr. More (*Regina City*), seconded by Mr. Lambert,

*Resolved*,—That the exhibits tabled by the Inspector General of Banks at the afternoon sitting be included as an appendix to this day's Minutes of Proceedings and Evidence. (*See Appendix L*).

Messrs. Paton, Coleman, and Lavoie were questioned.

In response to a question regarding views of the Canadian Bankers' Association on the proposed deposit insurance legislation, Mr. Paton tabled a paper entitled *Proposal for Deposit Insurance* copies of which were distributed to the members.

On motion of Mr. Monteith, seconded by Mr. Leboe,

*Resolved*,—That the two papers tabled today by the Canadian Bankers' Association, entitled *ASH Ratio Management—Proposed "Twice-Monthly" Averaging Technique and Proposal for Deposit Insurance* included as appendices to this day's Minutes of Proceedings and Evidence (*See Appendices M and N*).

At 10:10 p.m. the Committee adjourned until Thursday, November 10, 1966, at 11:00 a.m.

Dorothy F. Ballantine,  
Clerk of the Committee.





## EVIDENCE

(Recorded by Electronic Apparatus)

TUESDAY, November 8, 1966.

The CHAIRMAN: Good morning, gentlemen. We have a quorum. I will call the meeting to order.

I would ask for several motions for changes in routine proceedings before we continue with the order of business. First, I would invite a motion that the amendments to Bill C222 and Bill C223, tabled by the Inspector General of Banks at the afternoon sitting on Thursday, November 3, be made appendices to the minutes of proceedings and evidence of that date. Could I have a motion to that effect?

Mr. CLERMONT: I so move.

Mr. LEBOE: I will second that.

The CHAIRMAN: Are we agreed?

Some hon. MEMBERS: Agreed.

The CHAIRMAN: I would also invite a motion that the evidence taken at the afternoon sitting on Thursday, November 3, be made part of the official proceedings.

Mr. LAFLAMME: I so move.

Mr. GILBERT: I will second that.

The CHAIRMAN: Are we agreed?

Some hon. MEMBERS: Agreed.

The CHAIRMAN: Gentlemen, we will resume our consideration of Bill C222, an act respecting inspecting banks and banking.

Our witnesses this morning are from The Canadian Bankers' Association. Their principal spokesman is Mr. S. T. Paton, president of the Canadian Bankers' Association, and chief general manager of The Toronto-Dominion Bank.

I would invite Mr. Paton to present the brief on behalf of his group. Before doing so, I would also invite him to introduce those who are with him as witnesses and as assistants: Mr. Paton.

Mr. S. T. PATON (*President, The Canadian Bankers' Association; Vice-President and Chief General Manager, The Toronto-Dominion Bank*): Thank you very much, Mr. Chairman. I might, at the outset, say how pleased we, as an association, are to be here before you today. We will do our level best to be as helpful as we can in answering any questions which you may have for us. My associates at this end of the room, on my immediate right, are: Mr. Leo Lavoie, who is vice-president of La Banque Provinciale du Canada and also vice-presi-

dent of the Canadian Bankers' Association; on his right is Mr. J. H. Coleman, vice-president of the Canadian Bankers' Association also, and he is chief general manager of The Royal Bank of Canada; behind me and I will refer to them in order, starting at my far right: Mr. Gilles Mercure, assistant general manager of The Provincial Bank of Canada; Mr. Charles Slade of the Canadian Bankers' Association executive staff; Mr. Harvey Perry who is executive director of the Canadian Bankers' Association; and Mr. S. Sarpkaya also of the Canadian Bankers' Association permanent staff. The two distinguished gentlemen on my left here are Mr. William Hackett, general manager, investments of the Bank of Montreal, who was chairman of the main banking committee in our preparations for the bank act revision and for the Porter report; and on Mr. Hackett's left is Mr. Forrest Rogers, who is economic adviser to The Bank of Nova Scotia and chairman of the economists' committee of the Canadian Bankers' Association.

The CHAIRMAN: Before we continue, I think perhaps I should point out that he is a distinguished former citizen of Windsor, Ontario.

Mr. PATON: Gentlemen, in accordance with the suggestion from the Chairman of the Finance, Trade and Economic Committee that we prepare a summary of our brief, I have this in front of me, and with your permission I will read it.

Mr. Chairman, and members of this Committee, the brief of the Canadian Bankers' Association has been placed before your Committee and you will all have had an opportunity to peruse it. I will not repeat it now, but merely give an outline of our main arguments.

Bill C-222 proposes essentially to follow the Porter Commission's recommendation to remove the interest rate ceiling. We welcome this forward step but wish to emphasize that we do not see any net benefit to the public from the interim arrangements. We firmly believe that the removal of the interest ceiling now would be in the best economic interests of the public.

The association favours the new mortgage lending provision and the new provisions for debenture financing. These powers will improve the banks activities in the total Canadian financial picture.

We would, however, urge the Committee to consider carefully the new statutory reserve requirements. We agree with the Porter Commission and the new bill in lowering cash reserves on notice deposits to 4 per cent. We do not find that the raising of cash reserves to 12 per cent on demand deposits is desirable and we wish to draw to your attention that the net result of the new cash reserve requirements still leaves a considerable degree of discriminatory treatment of the banks relative to competing institutions. The secondary reserve requirement, which is introduced in the bill, is a measure of discriminatory treatment, and, in the opinion of the Porter Commission, unnecessary for an effective monetary policy.

In this same general connection, we urge that Canadian coin be considered as part of our primary reserves. It is so obviously cash yet not a part of our legal cash reserves. The new provision for half-monthly averaging of cash



reserves causes us concern because of the adverse effects it might have on the money market. No compensating advantage seems to go to the monetary authority.

Section 76, limiting banks to 10 per cent of the holding shares of a Canadian company, is, in our opinion, detrimental to the best and most enterprising development of financial services in Canada. Bank participation in other financial undertakings which help to fill gaps in our financial system and to encourage a much more competitive atmosphere, are favourable influences which we feel should be encouraged to continue. The restrictions in the bill would greatly limit the banks flexibility which is so necessary in our fast-changing world.

The disclosure of inner reserves of the banks and their year to year losses is without substantial benefit. The public interest, we feel, is amply protected by the present system of disclosure to the Minister of Finance. Disclosure to the public would affect our ability to take risks on loans and might unduly affect confidence in the banks when and if substantial losses occur.

This ends the matters formally considered in our brief and I would be very glad to answer your questions on these. I will also do my best to answer any other questions which you might wish to address to me as a practical banker and as President of the Canadian Bankers' Association; and, with your indulgence, I would also like to feel free to call on any of my associates, both those behind me and in the general audience, if I feel that they could better handle any particular questions.

That, gentlemen, is the summary of our brief.

The CHAIRMAN: Thank you, Mr. Paton.

Before the meeting began you indicated to me that you had some information which you could provide us on the nature and the function of the Canadian Bankers' Association. Perhaps it would be helpful to have this information now. It would put our discussion in the proper perspective.

Mr. PATON: Thank you, Mr. Chairman. I will be very pleased to do so. It is a reasonably lengthy document but I will read it verbatim. I had it prepared over the week end.

The CHAIRMAN: We can highlight some of the parts as we go along.

Mr. PATON:

I welcome the opportunity of giving a brief statement on the role of the Canadian Bankers' Association at the opening of our appearance before you.

This will serve to amplify and up-date explanations presented by my predecessors at previous revisions of the Bank Act.

The Canadian Bankers' Association is one of the oldest such organizations in Canada, having first been established in 1891. The immediate reason was the realization of a previous informal group of bankers following the revision of 1890 that a permanent body was needed to cope

with a growing number of problems of interest to the whole industry. The organization assumed its present formal corporate existence in 1900 under an act of the federal government. Many of its original functions in fact were entrusted to it by the federal government, prominent among these being the supervision and inspection over the banks note issue. It will be recalled that the office of the Inspector General of Banks was not established until 1924, and also that the banks were empowered to issue their own notes until 1935, when the Bank of Canada was established. This one aspect of banking alone would have required close co-operation between the banks and governmental authorities in the earlier days before formal governmental agencies were introduced. In time the banks through their Association developed activities of value to the banking industry, including an educational program for bank employees and a banking journal. From the beginning the Association also operated the clearing houses throughout Canada.

Today the Association has as its members the eight chartered banks of Canada, and any new chartered banks will become members at commencement of business. The Bank of Canada, the Industrial Development Bank and the Quebec Savings Banks are not eligible, since membership is defined as those banks listed in the Bank Act or chartered under the Bank Act. The core of the Association is the Executive Council composed of the general managers of the banks. The officers are the President and four Vice-Presidents, two each from Montreal and Toronto. The Association has two offices—one in Toronto and another in Montreal—and a total staff of some 30 employees under the charge of an executive director. There are also association committees of bank specialists who, in conjunction with the staff of the Association, carry out studies or conduct negotiations of importance to the banking system as a whole. The number of such committees will vary from time to time, depending on the range of issues requiring attention. There are also two sub-sections of the Association, one for the western provinces and another for the Pacific area.

One key to an understanding of the varied and extensive activities of the Association is the fact that on countless occasions throughout the year the banks are called upon, most frequently by government, to co-operate as a group in some new function to be performed or some new policy to be carried out. These requests are directed to the Association, and as a matter of convenience and efficiency are expected to be dealt with through the channel of the Association. Another key is that there are few businesses which operate to the same extent as banking as a closely integrated system in which a certain uniformity of procedures is essential for efficient performance. This aspect of banking accounts for a good deal of the work of the Association. Finally there is the fact that in any industry a good many activities affecting the progress of that industry can best be carried out on a group basis. This is the third key to an understanding of the Bankers' Association. I might briefly discuss each of these three headings in their order.

The first heading would be the meetings of the Executive Council of the Association with the Governor of the Bank of Canada and senior representatives of the Department of Finance. At these meetings matters of highest importance affecting the monetary and financial affairs of the country are discussed, and frequently during these discussions the co-operation of the banks in matters of urgent public interest is requested. Many of these matters are of a very confidential character, but I am sure that I would not be infringing secrecy if I mentioned that at our last Council meeting both the Governor and the Deputy Minister of Finance urged the fullest co-operation of the banks in the current Canada Savings Bond drive. Needless to say the banks are giving such assistance to the fullest possible extent.

At a lower level of importance is a wide range of subjects calling for study, discussion and sometimes protracted negotiation by the Association staff or committees or frequently both. Prominent among these are the long list of government guaranteed loan programs, where changes in forms and regulations are constantly taking place. Most of these programs are federal, but at this very time negotiations are underway with the Government of Quebec on a student loan program to parallel the federal program. This year the banks at the request of Expo are co-operating in the advance sale of passports, and the arrangements for having these available throughout the whole branch system required extensive negotiation and planning. Other issues of the recent past have included the shortage of coin, the Canada Labour Standards Code, centennial celebrations, legislation affecting bank pensions, changes in accounting and banking procedures of certain government departments, requests for publicity for certain government programs through bank branches, tax changes affecting the banks, and so on. This list could be extended indefinitely.

I might mention only two instances under the second heading. The most striking example in recent years was the adoption, after extensive study, of the magnetic ink system (MICR) of encoding cheques. With the move toward automated sorting of cheques, leading to automated accounting procedures, it would have been disastrous for both the banking system and the public if different systems of encoding had been adopted by the various banks. Uniformity of action was therefore essential. And of course the need for uniform procedures in other areas will increase as functions become increasingly automated.

Finally, I have said that the Association acts to serve the direct interests of the banking business in a variety of ways where group action is most logical and efficient. I shall simply list some of these:

One is education. There is a very extensive program in education. We have appointed a new Director of Education, Professor André Bisson, formerly head of the School of Commerce at Laval University, and he will be forming an Institute of Banking for Canada.



In 1967 we will be host to the International Banking Summer School. This school brings over 200 bankers from 50 countries and involves a heavy responsibility and an honour for the sponsoring country.

We have a permanent publication; it is one of the leading banking journals of the world, now being in its 73rd year of publication. We also publish a White Bulletin dealing with banking issues, which is widely used in university classes in money and banking.

In public relations we occasionally act for the banks where public relations are involved. This applies to Expo and other similar situations.

We provide a vast amount of information on developments of all kinds, such as new laws, regulations, jurisprudence, practices and policies, both in Canada and abroad, et cetera.

Robberies and securities—we are constantly working with the police forces throughout Canada in an endeavour to curb these.

Foreign exchange—we provide a service to the banks. We employ four foreign exchange brokers.

Clearing houses—as was mentioned above the Association has the operation of the 51 clearing centres throughout Canada.

Gentlemen, this has been rather lengthy and I will discontinue, sir. I hope you now have some idea of the functions and the purposes of the Canadian Bankers' Association.

The CHAIRMAN: Thank you, Mr. Paton. I think this additional information will be helpful. I would ask your group to cooperate with our clerk and have copies of the statement made and distributed today, if possible, so that we may be able to refer during our questioning, to some of the things you have said about the association.

I think we should now begin our questioning. The first person I have noted was Mr. Lambert. If the others will signify, I will recognize them in some reasonable order.

Mr. Lambert, would you like to start?

Mr. LAMBERT: Yes, Mr. Chairman.

Since the act which governs the chartered banks is the Bank Act, and since there is a repeated reference to the term "business of banking" in the act, I would like to have the benefit of your interpretation of what is "the business of banking". Is it conceivable to arrive at a legal definition, whether it is, shall we say, one which is a practice of the trade, or an agglomeration of a number of practices or functions in the commercial and financial market?

I have come to the conclusion that unless one is able to give a legal interpretation to such a phrase in a statute, which is part and parcel of the constitution of every bank, then, it should not be used. There must be some meaning to "the business of banking" and I am interested in arriving at a definition of "the business of banking".

Mr. PATON: Mr. Lambert, this, I would say, is a question which has engaged our deep and lengthy consideration, and it is one on which we have yet to arrive at the sort of answer which satisfies ourselves apart from being in a position to satisfy others.

The definition of "banks" or "banking" has been thoroughly studied and has been of concern in many countries for many, many years, and to our knowledge there has been no firm attempt, other than as the result of judgments handed down in one or two court cases, by any legislative body to define banking.

We, in our considerations prior to appearing before the Porter Commission and in our brief to the Porter Commission, recognized this difficulty in arriving at a definition, and implied to them that we would prefer, perhaps, to stay away from any prescribed definition of banking but rather look to the area where enough exemptions, or enough easing in this new Bank Act, would permit banks to be more competitive, and thereby remove some of the disabilities under which we are presently operating.

The Porter Commission's Report did come out with an attempted definition of a bank. Perhaps it is a question of handling this in two parts. If one could come out with a definition of a bank and then say that such bodies could perform banking functions such as are included in Bill C-222, perhaps that might be best. The Porter Report, without having the exact wording here, implied that they would consider that any depositing-gathering institution—taking deposits of 100 days, or less—would be doing a banking business, and would consider such corporations should come under an act which should be either the Bank Act or one related thereto.

Our association's stand at the moment is that rather than try to define banking we would prefer to see the general concept of the banking corporation, or the banking institution, applied universally across the country.

Mr. LAMBERT: I have the greatest difficulty, Mr. Paton, frankly, in, shall we say, trusting this hesitation in defining what is your business. For instance, under section 13, it says: "The bank shall not commence the business of banking . . ." In other words, what is its business, if you cannot define it? This is the point. I feel that if, perhaps, we can arrive at some general definition of "banking," without necessarily spelling out and dotting all the i's and crossing all the t's, we can get around a certain dilemma. The constitution of Canada grants to the federal parliament the exclusive jurisdiction of dealing with money and banking or currency. Therefore, one must understand what "banking" is.

The next step is that in passing this act, or its predecessors, we are dealing with banking, and surely we must know what we are dealing with; and I assert that, having been granted the exclusive jurisdiction, we pass an act, and those who would quarrel with the act must assert that there is another exclusive jurisdiction for controlling any of the functions which may be defined as "banking." It is not enough for them to say that there is a joint jurisdiction but it must be exclusive to the province; because jurisdiction with regard to any of the functions carried out by the banking system is not something which exists in a vacuum. It must be under the federal parliament.

That is why I feel that the banks themselves should be in a position to define, perhaps not exclusively but certainly in a general way, what is their business.

The CHAIRMAN: Before you answer, Mr. Paton, I just want to point out that you are free to call upon any of your associates to reply to a particular question, or to supplement your own comments.

Mr. PATON: Thank you, very much, Mr. Chairman. Mr. Lambert, I would say that we in the banking profession are very conscious of this anomalous situation, that we are permitted to carry on a business which no one can define, or has defined. I would suggest that ultimately some solution has to be found.

I also think that this will take considerable time, because in endeavouring to reach for a definition one has to be careful not to limit the functions that a bank might conceivably undertake, either as of now or perhaps have an opportunity of undertaking, as our country's economy develops. I am reasonably certain that it would take much more time than we currently have at our disposal to come to a decision on what the legal definition of "banking" would be.

Mr. ELDERKIN: Mr. Lambert, during the hearings in the last two weeks there was a court case referred to, where the judge gave a decision and tried to spell out "banking". It is already in the record.

Mr. LAMBERT: I am aware of that case, but Mr. Justice Primrose does not say there that there is an exclusive jurisdiction within the province. He really ducked the issue, as he did not have to face it, on whether there was not concurrent jurisdiction, and he simply said that, within the terms before him, he felt some of the operations qualified under the property and civil rights of the province.

This may be interesting, but the point is, that even though the treasury branch of the province of Alberta may exist under a function referable to property and civil rights, yet the functions which it performs also come under "banking" and would not be excluded from the jurisdiction of the Parliament of Canada.

This is the point I am making, frankly—to arrive at a definition of "banking" so that many of the near bank operations would fall under one big umbrella.

Mr. PATON: There have been various proposals, and we recognize that they have a good basis; however, our main consideration is that it is a question of supervision and regulation, and if that could be brought under proper control we, as a banking industry, would be reasonably satisfied to proceed—at least until the next decennial revision—on the definition of "banking" as outlined in the various sections of Bill No. C-222.

Mr. LAMBERT: That is all, Mr. Chairman. I just wanted to emphasize this lack of definition even among bankers.

The CHAIRMAN: That is a very important point. Do you have further questions, Mr. Lambert?

Mr. LAMBERT: No; I am quite prepared to pass.

The CHAIRMAN: Mr. Clermont, you are next.



(Translation)

Mr. CLERMONT: Mr. Chairman, the acting directors of the Bank of Western Canada, and of the proposed Bank of British Columbia stressed how important is the siting of the head office of a bank. They claim for example, that if a bank were established in British Columbia, with the head office in Vancouver, the borrowers would find their position, as borrowers, much improved. Mr. Coyne and Mr. Stevens, of the Bank of Western Canada, expressed the same view with regard to locating the head office of the Bank of Western Canada in Winnipeg. I would like to know the exact views of the Canadian Bankers' Association about this question, because I think that the banks now operate on a regional basis. Does this regional delegation of responsibility provide plenty of latitude to the people responsible, under the title, if I am not mistaken, of general manager?

Mr. LAVOIE: Mr. Clermont, as you said just now the chartered banks in Canada do operate on a regional basis. The three biggest banks have districts, and in each district there are general managers who conduct operations in the regional banks, as for example, the two banks in the Province of Quebec. We do have administration by section, where the operations are conducted by superintendents. The Head Office of the institution may be here or there but I do not think this a very important matter. The Head Office handles administration *per se*, but the operations are conducted regionally, and I am certain that each general manager of a bank responsible for operations in a region does everything he can to attract business in his region, so much so that the head office sometimes have to bring him under control because each regional manager is trying to attract the heaviest number of depositors and borrowers into his bank.

Mr. CLERMONT: When Mr. Coyne, was witness on behalf of the Bank of Western Canada he maintained that 75% of your branch managers had no freedom of action regarding credit.

Mr. LAVOIE: Mr. Clermont, I do not know if Mr. Coyne was well-informed regarding the present banking system. I can tell you that the banks operate this way, first of all through the branches, and the Branch Managers do have freedom of action. Above them are the general managers by regions, or and the superintendents of regions who do have considerable freedom of action in granting loans. Where the loans requested are too heavy for their competence, the loan requests at issue are forwarded to headquarters for review by the Board of Directors.

Mr. CLERMONT: Would it be indiscreet to ask you what is the extent of freedom of action given to the manager of an average sized branch bank at the present time. I know from experience that the freedom of action of branch managers has been depleted in recent months, but would the manager of an average branch bank normally be free to grant \$3,000 or \$5,000 credit on non-guaranteed loans, and if the loan is guaranteed, would the limit go as high as \$10,000 or \$15,000?

Mr. LAVOIE: When you decide what freedom of action you want a branch bank manager to have, you do not base your judgment solely on the branch but also on the qualifications of the manager, and when you have determined what his qualifications are, then you decide what shall be his freedom of action. The scope covered by his freedom of action ranges from the personal loan, the

guaranteed loan, the customers' bank bills. There are several different types of loan, and I wonder what you want to know exactly. Is it what freedom of action does the manager have in granting loans against personal collateral.

Mr. CLERMONT: What I mean is this. If a branch manager has some freedom to grant credit, the argument of the acting directors of the proposed bank is not nearly as strong.

Mr. LAVOIE: According to our statistics, 90% of the loans granted by the banks are granted within the field of latitude allowed to the managers.

Mr. CLERMONT: And again, I would ask you, in accordance with your experience, does it matter whether the headquarters of the banks, because at present the chartered banks all have their head offices in Toronto or Montreal, except for one bank which has its head office in Halifax, but whose operations are conducted almost entirely through Toronto. Would you not say, on the basis of your experience as a banker that the choice of Toronto or Montreal as site for head office means that the interests of the manufacturers and of the industries in a given province are neglected?

Mr. LAVOIE: I don't think it makes any difference. I am convinced that whether you have the headquarters in Toronto or in Montreal, as we have at the present time, does not greatly change the character of the banking operations in Halifax or Vancouver. Means of communication are readily available these days and I think that a regional manager or a superintendent can get in touch with his headquarters by teletype and get his answers back by teletype where he must consult in regard to some matter outside his competence.

Mr. CLERMONT: We have been told before this Committee that on certain occasions an industrialist or a business man from Vancouver or Winnipeg or Halifax or St. John's, Newfoundland, has been forced to get into an airplane in order to meet the bank managers or the bank directors, either at Toronto or at Montreal, in order to get a loan which he could not get at home.

Mr. LAVOIE: I do not see how that could happen, but there may be some other reason why the headquarters of the chartered banks are either at Toronto or in Montreal. Montreal and Toronto are the places where transactions take place, so, I think that banks would rather have their head offices of the banks in those places than in places like Winnipeg, because the money markets are much more alive in Toronto or in Montreal.

Mr. CLERMONT: And now another line of questioning, Mr. Lavoie, the President of the Canadian Bankers' Association has said that the Canadian economy could accommodate several new banks in Canada, chartered banks, that is. I think Mr. Coyne himself said that the Canadian economy could accommodate at least twelve new banks, twelve new chartered banks.

Mr. LAVOIE: I don't think the present banks are opposed to the setting up of new banks, I don't think the Association is either, I don't think that we are against the granting of new charters, no. We never have been.

Mr. CLERMONT: But would you not like some of the near-banks to be treated as true banks?

Mr. LAVOIE: You want to discuss the "near-banks"?

Mr. CLERMONT: "Near-banks" is not exactly a French expression, no, but—

Mr. LAVOIE: But it is a word which is current—

Mr. CLERMONT: All right, I will accept the word "near-banks"—

Mr. LAVOIE: But if the near-banks are willing to accept the same legal controls as those which apply under the chartered banks act, that is holding reserves in the Bank of Canada and applying for bank charters, it would then be a question for Parliament.

Mr. CLERMONT: In the brief which the Bankers' Association brought before this Committee, one of the objections that you expressed is to the effect that, maintenance of the interest ceiling in the manner recommended by Bill C-222 would make the bank a more flexible instrument in granting loans to small industries. Others claim that taking the interest ceiling off would increase the cost of industrial operations and so slow down Canada's economic development and possibly lead to accentuated unemployment in Canada.

Mr. LAVOIE: Well, the small borrowers have two sources of loans, either they get them at the banks or they can get them from other organizations, such as finance companies. So far, the 6 per cent ceiling that has been applied to the banks did stop us from engaging in a number of transactions which we would have liked to engage in. We might have been able to accommodate a certain number of customers whom we would have liked to help, but could not help because of the 6 per cent ceiling. As you know, the near-banks are competing for deposits with the banks and these deposits we have to observe the bank rate of 3 per cent whereas the near-banks, or trust companies can pay 6, or  $6\frac{1}{4}$  per cent on deposits. These institutions also lend out at considerably higher rates than do the banks. That is why we are asking that the six per cent ceiling be removed so that we can go out and make other transactions and help small industries.

Take for example the mortgage loans. Take the case of a merchant in a small community who wants to have a loan, say \$25,000 or \$30,000. Part of that loan goes to his working capital and part to his operating expenditures. If the bank could give him a loan at a reasonable rate, that would certainly enable him to improve his working capital and to continue his transactions and I am certain that this would help the small fellow, the small business man and the small industrialist in any community.

Mr. CLERMONT: Regarding the interest rate, have the banks not managed to evade the restrictions indirectly through mortgages? Have not the banks even bought shares in trust companies which themselves make loans?

Mr. LAVOIE: Mr. Clermont, the chartered banks can make mortgage loans under the National Housing Act and when the interest rate rose above 6 per cent, the chartered banks ceased making the loans.

Mr. CLERMONT: Yes, but do not the chartered banks have shares in trust companies, and do these trust companies not make mortgage loans?

Mr. LAVOIE: It is very difficult for me to answer you, I don't know whether other banks do or do not have shares in trust companies, but I do know that some banks, for example, the Banque Canadienne Nationale and the Royal Bank



of Canada, have bought shares in Roy Nat; Roy Nat is a company which makes long term loans, as you know.

Mr. CLERMONT: Let's suppose that the Bank of Montreal or the directors of the Bank of Montreal may also be directors of the Royal Trust. Are there not Royal Bank directors who are Montreal Trust directors?

Mr. LAVOIE: I doubt that the question of directors arises here. The issue is investments.

Mr. CLERMONT: But banks like the Bank of Montreal have shares in the Royal Trust and the Royal Bank has in the Montreal Trust, don't they?

Mr. LAVOIE: It is a rather difficult question for me to answer.

Mr. CLERMONT: I am not questioning Mr. Lavoie in his capacity as general manager of the Banque Provinciale, but he has been introduced to us as the vice-chairman of the Bankers' Association.

Mr. LAVOIE: Mr. Coleman has just told me something, he is the chief general manager of the Royal Bank and he says that they don't have shares.

The CHAIRMAN: You are quite right, Mr. Clermont, I think Mr. Paton would like to say something as he is President of the Association.

*(English)*

I think you were trying to get an opportunity to supplement Mr. Lavoie's answer to the subject.

Mr. PATON: Yes. Mr. Clermont, there were several questions some time back which I would have liked to supplement. I would like to say on the question of regional banking and the fact, as you implied, of banks having their head offices in Toronto and Montreal, I can assure you quite unequivocally that if there is any advantage or disadvantage to it, it leans on the advantage side, because with our geographical divisions under the relatively autonomous direction of the top men they are competing with each other's divisions to do their level best to bring their division out ahead of the others. This inevitably tends to giving more than a hundred per cent attention to the problems in their own area.

With regard to the joint directorship, perhaps, or an interlocking directorship, as there are in a number of cases of banks and trust companies, there is no doubt in our minds that this is not inimical to the welfare of the Canadian economy. These people are knowledgeable and influential people in their own line of business, apart from their directorates in the trust companies and banks and they serve a very useful and very helpful purpose in their representation on the bank board.

In so far as ownership of trust company shares is concerned, as has been indicated, this would be something for each individual bank to respond to.

*(Translation)*

Mr. CLERMONT: Mr. Chairman, may I come back to the question of interest rates? Through loans made to consumers, or by their personal non-guaranteed loans, have not the banks evaded the legal restrictions? Is it not a habit which is to be found among the banks? There is a rumour to the effect that certain banks lend, shall we say, \$10,000 to a borrower, and more or less make him leave a balance of \$1,000 out of the \$10,000, in the bank, so he pays the rate of interest

of 6 per cent on the \$10,000 but can only take advantage of \$9,000 of the \$10,000. Is that right, if so the bank has evaded the ceiling on the interest rates.

Mr. LAVOIE: The first question you asked, was about evasion of the interest rate ceiling of 6 per cent. It is known that banks do make personal loans at a rate of 6 per cent but to the 6 per cent insurance charges are added so that if the client dies before the loan expires, then the loan is wiped out. And then there are service charges, because, as you well know, Mr. Clermont when you enter a loan on the books, no matter what the amount, it is the same amount of work whether it is a million or \$10,000, and the more loans of this nature we have the more we have to increase the staff, so we have service charges. These service charges are not very high and may I assure you that they compare advantageously with those of other companies, independent institutions such as the finance companies, which conduct this type of operation. Regarding your second question, what were you enquiring about?

Mr. CLERMONT: I mentioned the fact that from time to time, the banks are supposed to make a borrower, who wants to borrow \$10,000, leave \$1,000 deposit in the bank but he pays interest on the total account, \$10,000. Therefore he only has the use of \$9,000. So I asked is this a current practice in the banks, or is it just a rumour that we hear?

Mr. LAVOIE: Mr. Clermont, your question is this: Suppose a customer wants to borrow \$10,000, from a bank, and he is told that he can only have \$9,000, and must leave the other \$1,000 in the bank. No, it is never done like that.

Mr. CLERMONT: How is it done?

Mr. LAVOIE: If the customer wants \$10,000, he gets \$10,000, he pays interest on that \$10,000 until he returns the loan. This question of making a client leave a balance in the bank is another matter. There have been many changes in the banking system. Previously companies or major customers left large deposits in the bank but they no longer follow this practice. They invest their funds either in trust companies or in short term loans so that they can get an interest rate of  $6\frac{1}{4}$  per cent, or higher. The banks want to get some kind of compensation for clearing. Let us say that a client draws a cheque on our branch in Montreal and we cash it in Toronto, but we may be able to debit his account, only two or three days later. He has had the use of the funds which the bank has supplied but the bank is out the amount during that time. So we ask our clients, depending on the volume of cheques he issues, to leave a certain deposit with us to cover his cheques in circulation. That is what actually happens.

Mr. CLERMONT: What do the bankers' association think of the idea, if I might refer to the clearing house, would it not be a good idea for the clearing house to be operated by the Bank of Canada? This was recommended in a brief to the Committee.

(English)

Mr. PATON: Mr. Clermont, if I might respond to that question, there have been some very decided misconceptions of the functions of the clearing house, and the clearing system. This is another of the subjects that we did a very thorough analysis of. I have a prepared memorandum here which gives a rather

elementary, perhaps elementary to bankers who have lived with it for 35 years, but a reasonably factual statement of what the clearing house is, and what the clearing system is.

The CHAIRMAN: Mr. Paton, if I may interrupt here, we appear to be entering into a new subject matter which may require to be adequately dealt with by a considerable series of questions by Mr. Clermont. I know he has given this subject a lot of study. It is my suggestion to the Committee that we try to keep each particular opportunity of questioning to the area of about 20 minutes, unless the Committee agrees to let the member continue. I would suggest, so that you would not feel that you are interrupted in this very important area of questioning, if perhaps we might pass on to the next member on my list and then you will have a better opportunity on the next round to pursue this area of questioning.

(Translation)

Mr. CLERMONT: I am glad to accept your suggestion, Mr. Chairman.

(English)

The CHAIRMAN: Now I would like to recognize Mr. Leboe.

Mr. LEBOE: Thank you, Mr. Chairman, I would like to follow up possibly some of the questions that have been put by Mr. Clermont in connection with some of the statements made by the witness.

First of all, I was interested in the situation regarding the head office of banks, particularly because it is often proclaimed in western Canada that fairly large loans have to be approved at the head office in eastern Canada. It is not a matter of the management altogether; it is a matter of the credit managers themselves who are responsible for making loans in the banking system. I said in the Committee before that in actual fact people have had to go to Toronto or Montreal as the case may be to negotiate fairly sizeable loans; whereas if the credit manager for the bank and the headquarters were in western Canada this would not be the case. Would one of the witnesses like to comment on this?

Mr. PATON: Yes, Mr. Leboe, I would be very pleased to. The discretionary limits as we refer to them in banking parlance, of the chief executive officers of these divisions are substantial. I think it is not divulging any secret at all to say that in some cases they reach up to half a million dollars. But it is obvious that there has to be some fulcrum, some central point, through which disposition of funds of this amount must be channeled. As we discussed last week with the governor of the central bank, there is a limit to the total money supply and each bank has a limitation on what it can lend.

If you will perhaps take a look going down the line, in the case of a bank that has 700 branches, if each of the managers has an average of say \$10,000 as a discretionary limit and he exercises that three times a day, there is \$30,000 he has loaned under his own limits and if you multiply that by your total of branches you can see that it runs into substantial figures. These discretionary limits increase as the seniority of the officer increases until they get up to the substantial figures that I mentioned earlier. Basically, this is the main reason why there has to be a central authority at wherever the head office is located.



It is true that on amounts in excess of the limit that the individual executive officer has, applications for credit in these amounts have to come to head office wherever it is located. But it is the exception rather than the rule where the individual requesting a loan has to accompany the credit application. There are many occasions where a firm or a corporation, or an individual applying for a loan requests the opportunity to, perhaps, get to know the head office executive people well, many of whom have served in these various divisions in the country; it is not a situation of a power sitting right on top putting thumbs down on the recommendations and applications for credit. Rather it is a central point for synchronizing the total lines of credit that are requested, for keeping each bank's own loaning function in reasonable relation to its liabilities and at the same time serving the needs of Canadian corporations and the Canadian public in the most equitable manner possible.

Mr. LEBOE: Mr. Chairman, I think this is good sound business practice and I think that it only points out the argument that the Bank of Western Canada had, and the Bank of British Columbia, that there are advantages to the people in those particular areas if the head office could be in that particular area. I think you have answered the question very well, sir, and have answered it in the positive.

I would also like to follow up a little bit on the matter of the 6 per cent since it was mentioned. I would like to ask the witness, in his view, what is the difference in the cost of the money that is being loaned out by the banking system compared to the cost of the money that is being loaned out by the so-called other institutions. Have you any comparative figures which would give some direction to the Committee because when you are talking about raising the ceiling of 6 per cent there are some of us who have not made up our minds and are looking at the thing and trying to look at it very objectively? I think the overall picture will be affected by the cost of the money, actually to the institution, as it relates to the lending out of this money and getting returns.

Mr. PATON: I doubt whether we have these comparative figures, Mr. Leboe. Certainly we would not have any knowledge of what the cost of money is to the other competing institutions, or as the governor referred to them, non-bank financial institutions.

Mr. LEBOE: I am not sure what the banks pay for deposits at this particular moment, the interest they pay, is it  $2\frac{1}{2}$  per cent or 3 per cent, but anyway, the other financial corporations pay over 6 per cent to get deposits lodged with them.

Mr. PATON: The major portion of our loanable funds comes from our savings and notice deposits and our demand deposits. I do not have the average to show the relationship between the two at the moment but on our savings deposits at the present time we pay at the rate of 3 per cent. This has been unchanged I think since 1954. No, I am sorry. It was  $2\frac{3}{4}$  June 1st, 1961, and in July 1962 it was 3 per cent. On demand deposits we pay no interest. These are operating funds largely in the accounts of the corporations and business people. On other notice deposits at the current time, if we do compete at all, we have been paying in excess of 6 per cent for amounts ranging anywhere from 60 to

180 days and the rates vary. This means that the average cost of our funds to the banks is somewhere in the neighbourhood of the region between these two amounts.

Mr. LEBOE: On this basis alone it would appear to the average individual on two counts, that the banking system gets the money that they are loaning out at less cost than the so-called other financial institutions. We will have the trust companies before us at which time I hope it will be our privilege to delve into the matter of their costs because we have to have something to gauge our opinion on if we are going to be fair and logical in assessing the release of this 6 per cent ceiling. The fact is that the deposit liability that is created when a loan is made becomes an interest bearing instrument; the note that is left at the bank becomes an interest bearing instrument on which no interest is paid. The only part of the interest which is relative to this is the amount of money that is lodged with the Bank of Canada as a cash reserve, and the relationship between the two does give, in my view, an advantage to the banking system in this regard. Would you care to comment on the statement that I have made? I do not want to put words in your mouth. I am just trying to make sure that you understand what I mean.

Mr. PATON: I do, sir. I am just afraid this might well get into a lengthy discussion.

The CHAIRMAN: I will be prepared to terminate it.

Mr. LEBOE: I think this is true but I think this is considered by the Bankers' Association as one of the most important elements of your brief, if I understand the brief.

Mr. PATON: The simple situation, as I see it, Mr. Leboe, is that this loan that we make does not automatically go in as a deposit and stay as a deposit. It is out very, very quickly.

Mr. LEBOE: Any bank would be very foolish to lend money which would lie idle in the bank.

Mr. PATON: I would be very foolish in the first place to loan money to a borrower who would be foolish enough to do that.

Mr. LEBOE: Just on this point, I do not want to interrupt your answer, in order to keep my mind clear on it, in the whole banking system when there is the ability, because of the reserve system, for the banking system to increase the money supply and as a result this particular bank does increase the money supply, at this particular point—and other banks will do the same thing—a goodly number of these deposit liabilities that have now been created, and there will be cheques written on this particular account, surely will become deposits in other banks, and vice versa, so that there will be a revolving situation where there will be returns of the savings deposits as a result of the total increase in the money supply of the nation.

The fact that I write cheques on this account after I have borrowed money does not mean that we have reduced the money supply of the nation at all, because we have not, have we? Therefore, the money supply of the nation is there and, also, although the individual draws all of his money out of the account, that he has borrowed, where he has created the deposit liability, the

note still bears the interest right up until the day of maturity for the full amount. So the bank is actually collecting the amount of money in interest charges on that loan, whether he draws the money out or leaves it lying in the bank. He certainly is not going to leave it lying in the bank, as you said. Is it not true that it is not as bleak as perhaps the Governor of the Bank of Canada was trying to make me believe it was the other day?

Mr. PATON: I would have to agree with the Governor. I do not know how bleakly you interpreted his comments, but I have to agree entirely with what he said last week and he said it probably much more effectively than I could.

There is simply no magic about banks lending money and taking in deposits. No matter what I do during the year, from one year to the other I know that at the end of October when my fiscal year ends and I have to produce a financial statement for every dollar that is owing to me through loans, I owe to one of two people, my depositor or my shareholder. If I was free to go out and make the loans and thereby increase my deposits that situation would be astronomically high. The simple fact is that through the Governor of the Bank, the Bank of Canada dictates as to what the total money supply is going to be in the country at any one time. The banking system is one group of people involved in it. The near-banks and other groups of people are involved in the actual disposition of that increase in money supply. There are many people grasping for it, and the only way I can make a loan to you is to go out and get somebody interested enough to put a deposit with me.

Mr. LEBOE: If I make a loan, borrow money at the bank, that particular loan that I take out does become a deposit if you have the reserves with the Bank of Canada to make that loan to me.

Mr. PATON: It does become a deposit liability of that bank.

The CHAIRMAN: You are not suggesting you are only loaning out the actual deposits of savers?

Mr. PATON: Not necessarily of savers. If you look at a bank statement you will see that they hold deposits of, let us say, \$3 billions between savings and demand and you will see that is divided up into investments, securities of X amount and loans of X amount. You have two sides of the balance sheet, liabilities and assets.

Mr. LEBOE: I think this is understood. But, we are not on the same channel here and I would like to express this opinion. You are talking about the end result and I am talking about the principle and the operation of the mechanics. It is like the planer,—I used to be in the lumber business—you put a board in there and if the knives are dull it comes out all woolly, but the board goes through just the same.

Mr. PATON: I am paid on end results, too.

Mr. LEBOE: Yes, I realize that, but on this particular point I am getting at the operation of the situation regardless of whether you make money or lose money at the other end. When we are dealing with the trust companies and other financial institutions, we want to be able to assess, with some degree of intelligence, exactly what we are going to do with this Bank Act. I hope this is our objective. In this particular case where the money supply is increased



through loans, it does appear, that—outside of the other costs to the bank—to us, to me at least, there is available to the banking system two things. They are limited by their reserves, of course. The other thing is that they have available to them cheaper money to loan out because of the banking system than the other institutions have in their efforts to get deposits. In other words, if they pay over 6 per cent for all of their deposits, and the bank gets deposits for less than that amount of money, then it seems to me there is to the average individual, a difference.

It is the principle of the operation that we are after here. You can sharpen the knives on the planer if you have the machine, but, if you do not know what the machine is and how to handle it, you are not going to be able to make the adjustments that are going to be best for the people of Canada.

Speaking of the principle, and not whether you make money or not, would you not say that the banking institutions have the privilege, having regard to the reserves they have with the Bank of Canada, of course, of creating credit, or creating money, which is the same thing.

Mr. PATON: No, sir, I would not say that.

Mr. LEBOE: You do not agree that they have?

Mr. PATON: I would take the stand that their position is exactly the same as any other deposit gathering institution.

Mr. LEBOE: Then you would differ with the Governor of the Bank of Canada when he said, in answer to a question from someone on the other side here the other day, I believe it was Mr. Gilles Grégoire, when he referred to the catastrophe that would be envisaged by the Bank of Canada making a direct inflow of capital to the tune of \$500 million. If you cannot create credit in the banking system—what you were telling me just now—this catastrophe that was spoken of by the Governor of the Bank of Canada certainly could not exist because the money supply could not increase. Now I want to ask you this question; if there were no chartered banks in Canada today would you be able to tell me exactly what procedure the Bank of Canada would use to increase the money supply of the nation, if it wanted to do so and there were no chartered banks operating under the reserve system?

The CHAIRMAN: No chartered banks at all, or none operating under the reserve system?

Mr. LEBOE: No chartered banks operating under the reserve system we have now.

Mr. PATON: I cannot envisage such a situation.

Mr. LEBOE: Well, if you could envisage such a situation, could you tell me how the Bank of Canada, if you do not create credit, could possibly substantially increase the money supply in a matter of weeks or days?

Mr. PATON: I think the answer is—I still could not envisage even an alternate to banks, there might be Bank of Canada branches, going on your hypothesis—the basic manner in which the Bank of Canada governs the money supply is by their market operations, by buying or selling securities. If the Governor went into that in considerable amounts he could still create the same effect—

Mr. LEBOE: We understand that.

Mr. PATON: —for the public, even if there were no chartered banks in existence.

Mr. LEBOE: Yes, but the point he was making the other day was that if he issued \$500 million it would not stop at that. It might run up to eight times that. Now where does the other money come from if the banking system does not create money?

Mr. GRÉGOIRE: Can you answer the question?

Mr. PATON: No, Mr. Grégoire, I do not think I can possibly answer it. I do not know if I can answer the question to the satisfaction of Mr. Leboe. I have my own thinking with respect to that. I think the Governor of the Bank was referring to some—

Mr. LEBOE: It seems to me it is so simple; money does not grow on bushes. If it does it would like to find the money bush. Therefore, if money does not grow on bushes it has to come into existence. Now the Bank of Canada says if they put out \$500 million it does not stop there. The banking system increases that amount of money by X number of times according to the reserves that are set by statute and by what we call persuasion. Therefore, with the two together the money supply is increased by the banking system. Now how can you increase that money supply in the banking system without creating money?

Mr. PATON: Mr. Leboe, let me put it this way. I could not possibly envisage the Governor of the Bank of Canada operating the Bank of Canada in such a way that suddenly he would have to inject \$500 million multiplied by this wonderfully magic number that we talked about last week. Any fluctuations in the money supply in a well-operated system, as ours is, is on a graduated basis.

Mr. LEBOE: Excuse me for interrupting, but we are back into results now and I am not interested in results. I am interested in the mechanics.

The CHAIRMAN: Well, Mr. Leboe, since possibly 20 minutes have elapsed it might be useful to let Mr. Paton ponder the implications of your questions and return to this area refreshed.

Mr. PATON: I think, perhaps, I might get somebody from our association who is more expert than I am in this subject.

The CHAIRMAN: I repeat, as I said before, that the witness is entitled to call on others associated with him to answer any question. Before passing to the next witness I would like to ask Mr. Paton a question myself.

I understood that you have made a comment, sir, that it would be foolish for the bank to lend money which would remain on deposit. Do I understand that you made a comment on something of that nature?

Mr. PATON: I said I would be foolish to lend money to a borrower who was foolish enough to leave it lying in my bank without getting any return. That was the import of my remark.

The CHAIRMAN: If that is the case, sir, why do you insist on compensating balances?

Mr. PATON: If I were to answer that question I would be admitting that we insist on compensating balances. This is one method of recovering costs. Compensating balances is a long standing method by which banks have recovered costs.

We have had compensating balances for many, many years in our current accounts. The activity in the current account reflects the amount of the balance that is held in relation to the number of cheques issued on the account.

Compensating balances in other cases are also used in relation to credit accounts, and the cost of operating loan accounts. Compensating balances have been, and are required in the form, perhaps, of heavier balances in the account. In other words, the compensating balances in the operating accounts have been increased to cover cost of other factors besides the operating accounts.

The CHAIRMAN: You are not disagreeing with me when I suggest that the banks do require compensating balances in loan accounts?

Mr. PATON: Not necessarily in loan accounts. Compensating balances cover the over-all cost of operating the account, which includes the loan sector.

The CHAIRMAN: Have requests for these balances been increasing in the last year?

Mr. PATON: Yes, I think, that would be a reasonable assumption. They have been increasing simply because the bank's operating costs in every field have been increasing substantially.

The CHAIRMAN: Would you say this is general for all the chartered banks?

Mr. PATON: I think it is a matter of degree, Mr. Gray. I would say in general that compensating action has been taken by banks in connection with the operation of their accounts that perhaps might take the form of an additional balance in the account, or perhaps might take the form of a special service charge, or some other commitment, for a line of credit or loan account.

The CHAIRMAN: Just one final question before recognizing Mr. Monteith: Have these compensating balances or service charges been at the same amount, or level, for all the chartered banks with respect to the customers for whom they request them?

Mr. PATON: No, sir; I would say that the practice of each individual bank is unique to its own operation. There may be a similarity, there may be uniformity, but the manner in which they receive their charges is handled entirely individually by each bank.

The CHAIRMAN: Would you say, then, that the customer of one bank who is not satisfied with the balance or service charge requested of him would be able to go to another bank with, often, a more competitive arrangement, in the same community?

Mr. PATON: There are no restrictions on any bank customer going from one bank to the other.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): What would be the result?

Mr. PATON: You are implying judgment much beyond my capabilities, Mr. Cameron. I could not speak for the other banks.



Mr. CHAIRMAN: We will leave that question to simmer a bit, and we will pass on to Mr. Monteith.

Mr. MONTEITH: Mr. Chairman, I only have a very brief question. Later on I would like to get into some of the technical aspects of the report of the Canadian Bankers' Association which I have read. Mr. Paton made a statement earlier in response to a question from which I gathered that he did not see anything wrong with the granting of additional bank charters.

Mr. PATON: I think Mr. Lavoie answered that question, but that would be my feeling, Mr. Monteith.

Mr. MONTEITH: There are no reservations there, as long as the bank is properly set up according to the Bank Act?

Mr. PATON: As long as parliament provides the necessary authority, the banks have, at no time, been opposed to new banks coming into the picture on the basis of private ownership and efficient organization.

Mr. MONTEITH: This is really an aside, Mr. Chairman, but I suppose this is the reason there was no representation before this Committee when the bank of western Canada was being considered.

Mr. PATON: We did not make any representations. We felt that it was not incumbent on us to do so. It would not have been proper to come and oppose it.

Mr. MONTEITH: Mr. Chairman, I was hoping to follow another line of questioning, but I am not too sure whether or not some of this information may not have been given by the Governor of the Bank of Canada, or by Mr. Elderkin, in previous evidence.

I think the last minute I have here of any meeting—incidentally, my apologies for being absent from the Committee for such a lengthy period, but it was beyond my control—is for October 18th and 19th. Have you any idea when more up-to-date minutes will be available?

The CHAIRMAN: I can assure the Committee that I am making every effort I can put forward to accelerate the printing of these minutes. This is a matter not too much within the control of the Chairman or the members of the Committee themselves.

The delay in printing these minutes arises, in my opinion, out of the lack of adequate reporting services for the committees in general, and I think I would like to take this opportunity to state publicly that those in charge of the reporting services—I am not referring to the staff members who are doing their best, but to those who are responsible for making decisions about increasing the size of the services and the facilities have an obligation to the members of the committees and, therefore, to parliament—should have them reach the level necessary to match the work of the committees as soon as possible. I thank you for raising the point and permitting me to make this comment.

Mr. MONTEITH: If this line of questioning has been pursued before, I do not want to repeat it.

The CHAIRMAN: I invite you to begin, and if it appears that it has been dealt with, I will stop you.

Mr. MONTEITH: I will be very happy to have you stop me. Mr. Paton, when a bank starts in business, they have so much subscribed capital. What is the next step when they open their doors? Can they loan part of this capital immediately?

Mr. PATON: It has been so long since a new Canadian bank has started, Mr. Monteith, and I have never participated in one, it is a question I have to think about.

The bank has capital, and first of all it has to attract deposits. I would suppose that the interested parties in the bank, the directors and their associates, their relatives, would probably be among the initial depositors of such a bank. Then the bank, having started, with whatever deposits and corporation business that it has—I know I am getting myself into a great problem area here as to which comes first.

Mr. MONTEITH: It is a very elementary question, I presume, to you, but the bank we will presume has just opened its doors. It has some subscribed capital, a few million dollars or something like that. Then it has some depositors, the directors and friends they have influenced to open deposits. How does it get its currency?

Mr. PATON: It draws its currency, its till money, as we refer to it, from the Bank of Canada.

Mr. MONTEITH: In return for what?

Mr. PATON: They would have to—this is the initial issue of currency that they take in.

The CHAIRMAN: If I may interrupt here, I think the line of questioning is quite proper, but if I may say so with all respect, Mr. Paton, it is obvious that you are not old enough to reach back to the beginning.

Mr. PATON: How am I going to get anybody?

The CHAIRMAN: No, what I was going to suggest was that you may want to consult with your professional advisers.

Mr. MONTEITH: I will be glad to leave it at this for the moment.

The CHAIRMAN: Your questions are perfectly proper, but it may well be that we are asking Mr. Paton to deal with an area in which he is not in a position to be readily familiar with as he is with the day to day operations of existing banks.

Mr. MONTEITH: Being a layman, I would just like to know in this respect how a bank starts, where it gets its money, its currency, and how it deals subsequently with the Bank of Canada, and all this sort of thing.

Mr. PATON: We have done a great deal of preparation for these hearings over the last five years, and this is one subject and one question that we have not considered at any time, but we will take notice of it and come back to it.

The CHAIRMAN: We would like to suggest, Mr. Monteith, that Mr. Paton consult with the professional staff of the association and with Mr. Elderkin and he might come back at the next round and give you a detailed answer because I

want to stress, your questions, in my opinion, are firstly in order and proper at this time.

Mr. MONTEITH: Well, that is all I have for the moment.

Mr. LEBOE: Mr. Chairman, I move also that special mention be made of the influence of that chartered bank opening up its doors, the influence of the individual who walks in and creates a deposit liability by borrowing money from the bank.

The CHAIRMAN: We should give you the opportunity of dealing with that yourself.

Mr. LEBOE: I would like to get it all together if he is going to get this much.

The CHAIRMAN: Well, I would like to recognize Mr. Gilbert at this time.

Mr. GILBERT: Mr. Chairman, maybe we could direct our minds to the brief that was presented to the committee and I direct your attention to page 2 where you set forth the ten year review of the banks and the necessity of providing proper safeguards, and at the same time the requirement of adaptability and flexibility with regard to legislation. Now, have the Canadian Banktrs' Association any views with regard to shortening the period concerning the review of the Bank Act?

Mr. PATON: No sir, I think that we consider ten years still as a reasonable time. For the benefit of the Committee I think we all know that in the year 1900 we were offered permanent charters and we declined them. The basis was that we felt the decennial review was beneficial both to the banks and to the economy of the country. I think probably the only reservation I have is that this decennial revision not be stretched out interminably to twelve years or thirteen years.

Mr. GILBERT: Suppose the near banks had a greater growth than they have had in the past few years which has been extensive, and they are not under the Bank Act, would ten years be too long to review the situation?

Mr. PATON: It could well be if we were inhibited by a similar Bank Act as we are operating under today. We feel that the Bank Act Bill No. C-222 is an improvement in this respect however. We are not quite so sanguine about it as perhaps the Governor was last week when he intimated that he could not see in the foreseeable future,—certainly not within the ten years, any continued progress of near banks sufficient to concern him. Any greater progress that near banks make in relation to ours is a concern of ours and perhaps in ten years—we might live to rue the suggestion that we do not shorten the period. However I think at the moment our feeling is that ten years is adequate.

Mr. GILBERT: Thank you, Mr. Paton, I wonder if I could direct your attention to page 3 with regard to the interest rate; do the banks categorize their different types of loans—business loans and consumer loans, mortgage loans? Are these the three categories?

Mr. PATON: Well, we provide the Inspector General with quarterly classification of loans which reaches I think into some 8 or 10 major subdivisions then we sub-categorize these. To provide the detailed information to the Inspector General. That is done on a monthly basis.



There are four major components: the first is government and other public services; the second, investment dealers and brokers; the third, personal loans; fourth, agricultural, industrial and commercial: agricultural, industrial and commercial, carry eight subdivisions. The personal loans carry two subdivisions with six and sections; Altogether we make a pretty thorough breakdown of our loan portfolios for the government.

Mr. GILBERT: What are the sections of the personal loans, Mr. Paton?

Mr. PATON: We have a No. 1 Section: individuals for other than business purposes; (a) on the security of Canada savings bonds at the agreed rate of issue; (b) on the security of marketable stocks and bonds. And our second category is individuals for other than business purposes; (a) for home improvement under the National Housing Act; (b) on the security of motor vehicles; (c) on the security of other household property; (d) repayable by installments not elsewhere classified; and (e) repayable otherwise, not elsewhere classified.

Mr. GILBERT: Do you think it is possible to make this breakdown of the different types of loans available to the Committee?

The CHAIRMAN: These are published I believe. Mr. Elderkin could you inform us on this?

Mr. ELDERKIN: Published annually, yes, on September 30 each year.

The CHAIRMAN: Mr. Elderkin, could I ask you whether with the co-operation of the clerk you could make this information available to us?

Mr. ELDERKIN: Yes, it is in *The Canada Gazette*.

The CHAIRMAN: *The Canada Gazette* is not exactly a magazine of popular circulation. Could you see that a copy was made available for the use of the Committee hearings.

Mr. ELDERKIN: Yes.

Mr. GILBERT: I wonder if you could look at paragraph (c) on page 3, where you are talking about the discrimination against borrowers such as small business which, if they obtain funds at all, must turn to other lenders, and the key words are "other lenders", and a few lines down you talk about sheltering high cost lenders from effective competition. To whom do you refer as "other lenders"?

Mr. PATON: Mr. Gilbert, these are quotations from the Porter Commission you refer to. These are the Commission's comments, so when you say—

Mr. GILBERT: You have adopted them.

Mr. PATON: Yes, but I just wanted to say that these are not the comments particularly of the Canadian Bankers' Association. We do not disagree with them, but they come from the commission. As to the other lenders, basically I would say that these lenders to whom people are forced to go through their inability to get loans from the banks as a result of the ceiling, are in the main the instalment finance companies. I think perhaps that is the proper answer to your question.

Mr. MORE (*Regina City*): Would credit unions be involved in these other lending institutions?

Mr. PATON: Yes, though I am not so sure to what extent their loans are addressed to small businesses, Mr. More. I do not think they do this type of lending very much and again I am going on not to define information. I think basically we are looking at instalment finance companies who are quite active and who have increased their activities in this area recently.

Mr. GILBERT: Do the Canadian Bankers' Association members agree as to the rates of interest that are to be charged in the different categories that you enumerated?

Mr. PATON: No, sir.

Mr. GILBERT: Do they discuss them?

Mr. PATON: Yes sir, they discuss them, very informally.

Mr. CHAIRMAN: Go ahead Mr. Gilbert.

Mr. GILBERT: Mr. Chairman, with regard to clause 138 of the new bill, which refers to prohibited agreement, it says:

138. (1) Except as provided in subsection (2) every bank that makes an agreement with another bank with respect to

(a) the rate of interest on a deposit, or

(b) the rate of interest or the charges on a loan, and every director, officer or employee of the bank who knowingly makes such an agreement on behalf of the bank, is liable to a penalty of five thousand dollars.

Against whom is that provision directed?

Mr. PATON: Against whom is it directed? It can only be directed against one group of institutions; the people who are chartered under the—

Mr. GILBERT: What you are saying is that it is not directed against the Canadian Bankers' Association.

Mr. PATON: I am sorry. I was **not** differentiating between the two. The bankers' association as such has no participation whatsoever in the question of interest on loans. I would like to make that clear. I thought you were referring to the Canadian banks discussing rates. The association is not involved in any way, shape or form.

Mr. GILBERT: I wonder if I could turn to page 7 of your brief. It is with respect to mortgage lending. Now that the banks will have the right to lend directly they have two categories. They have the N.H.A. and direct lending themselves on mortgages. I understand that the N.H.A. rate is  $6\frac{3}{4}$  per cent.

Mr. Elderkin, in his evidence, said that if we were to adopt the new formula set forth in the bill the bank interest at the moment would be 7 per cent and in the spring it would be  $7\frac{1}{4}$  per cent. Now, how is this going to affect the bank rates with regard to mortgages on the understanding that conventional mortgages at the moment are  $7\frac{1}{2}$  and 8 per cent? How is it going to affect the N.H.A. loans at the banks now participate in?

Mr. PATON: Well, I think possibly as a result of the completely anomalous situation which exists at the present time we are looking at a 6 per cent rate

which is both the low and the high. The 7 and the  $7\frac{1}{2}$  per cent rate that Mr. Elderkin referred to is the proposed ceiling rate. It would not be the minimum but the maximum. It is quite conceivable that a  $6\frac{3}{4}$  per cent mortgage rate or 7 per cent mortgage rate would be quite attractive to the banks. I think the important thing to stress is that this is the raising of the ceiling rather than the raising of the prime rate to that area.

There are no restrictions in our participation in N.H.A. mortgages. In the act there will be a restriction on our going into conventional residential mortgages related to amounts but there would be no restriction to the banks going into N.H.A.

Mr. GILBERT: I notice that on page 7 you say: "In such circumstances it would not be helpful to anyone to build up unwarranted expectations as to the volume of new mortgage funds that can be provided in the relatively near term." What is meant by that?

Mr. PATON: This comment is made in the light of current monetary conditions. The bankers as a group are well learned up at the present time and it could hardly be anticipated that they would divert a large pool of funds to this new area of lending to the detriment of our existing borrowers whose demands are presently very substantial.

Mr. GILBERT: So the public cannot have high hopes of active participation at the moment in the mortgage lending field by the banks.

Mr. PATON: That perhaps is just half their story. If the ceiling is completely removed, as we would like to see it, this would facilitate and encourage our ability to participate in competition for deposits. The more deposits we can take in the better we will be able to participate in this new form of lending.

Mr. GILBERT: Mr. Chairman, I have just one final question and it is with regard to page 11 of the brief.

Mr. PATON: Mr. Gilbert, may I just go back to one point there to clear it up? Our residential mortgage lending will be free of the ceiling, even the new ceiling, if it is on a conventional basis. I regret I did not clarify that.

Mr. GILBERT: This is what disturbs me, Mr. Paton, conventional mortgages at the moment are  $7\frac{1}{2}$  and 8 per cent and you will now be provided with the opportunity of participating in the conventional and the N.H.A. The N.H.A. are fixed at  $6\frac{3}{4}$  and the conventional are going to be  $7\frac{1}{2}$  to 8 per cent. The possible decline in the amount of participation in the N.H.A. loans worries me.

Mr. PATON: Vis-à-vis the conventional?

Mr. GILBERT: Correct.

Mr. PATON: Well, the conventional will still be better mortgages. You will still have the government of Canada's guarantee.

Some hon. MEMBERS: You mean the N.H.A.

Mr. PATON: Did I say conventional? I am sorry.

Mr. GILBERT: On page 11 you are referring to the limitations on bank participation in other corporate ventures. At the bottom of page 11, in the last sentence, you say: "For example, some of the newer ventures in which banks



have been taking an active or leading part providing services in the areas of mortgage and real estate finance and in developmental financing of various types, many of which were not available before." What ventures are you referring to with regard to the bank taking an active or leading participation?

Mr. PATON: Mr. Gilbert, two names particularly have been mentioned at these hearings. There are others but these two would possibly serve. One was Roy-Nat and the other was Kinross. Now, both these corporations have filled a void or a partial void in certain areas of financing and I think it is indisputable that they have benefited the economy in the relatively short time that they have been in existence.

Mr. GILBERT: Is it the feeling of the Canadian Bankers' Association that they should be given special treatment or preference because of this role that they have played?

Mr. PATON: They should not be given special preference but the participation of the banks in them, we feel, should not be interfered with, as is proposed in this bill.

Mr. GILBERT: Well, if other banks participated in this same activity should they be given special preference; that is, other banks which have not participated in the past?

Mr. PATON: Certain banks, a number of them, have shown initiative in this respect. Two names have been mentioned but there are several others. I think it is unfair, perhaps, and the association thinks that it is unfair, that these banks should be penalized for the aggressiveness or progressiveness they have shown. I also think we would prefer to see such ventures still remain open for participation by banks generally. Between now and ten years from now we have no knowledge of what opportunities might come up that would be extremely beneficial to the country. It is felt that if there has to be legislation along these lines, at the very least it should not be made retroactive. We still feel it would be good for the economy, and it can be controlled properly, to permit banks to have freedom to invest and participate in such ventures.

Mr. GILBERT: Thank you, Mr. Paton. I have one more short question.

What provision in the Bank Act sets forth the right of the banks to impose service charges?

The CHAIRMAN: I think it is Section 93 (3).

Mr. PATON: Mr. Gilbert, it is on page 77, Section 93 (3).

Mr. GILBERT: That talks about an express agreement between the customer and the bank. When is that express agreement entered into?

Mr. PATON: Basically, I think in connection with individual accounts, this is entered into by agreement when the signature card, authorizing the opening of an account, is signed. There is a service charge clause.

I am going back a few years, since I have been in branch work, but I imagine it is still the same. The customer agrees to pay the charge assessed by the bank.

Mr. GILBERT: Under the new legislation, there is going to be a disclosure of interest rates chargeable. Is that not right?

Mr. PATON: Yes, I think there is some discussion going on with the provincial authorities in connection with the disclosure of interest rates at the moment.

Mr. GILBERT: Mr. Paton, is it feasible to have included in that disclosure, the percentage of the service charge rate with regard to the loan?

Mr. PATON: Are you referring to the consumer finance loans?

Mr. GILBERT: Yes. In other words, suppose the consumer finance loan, we agree, is at 8 per cent for a loan, but then there is the imposition of the service charge; can you translate that service charge in terms of interest rates?

Mr. PATON: Mr. Gilbert, I think I can assure you right at this point that the representatives of the banks have never opposed disclosure of interest rates. We are quite prepared to do so at any time, provided a suitable formula can be obtained. The mathematicians tell me that there are five different ways of arriving at a particular effective rate of interest. This has been the subject of discussion by provincial consumer credit associations, there is a problem with respect to getting a uniform approach to the problem, but once that is solved, we would be quite in favour of disclosure, provided all other lenders would do so.

Mr. GILBERT: Well, maybe you would be taking the initiative in this.

Mr. PATON: We certainly have nothing to be ashamed of in the rates that we charge, my concern would be that perhaps we would be looked upon as the bad boys if we were the only ones having to produce the interest rate. This is why we would like to see it made applicable to all. If it can be made workable for the banks, surely this can apply to—if not all lenders—certainly other groups of lenders.

Mr. GILBERT: I agree with you.

The CHAIRMAN: On that positive note, I would suggest that we recess. In any event, Mr. Gilbert, I think you had the initial 20 minute period. We will now recess to 3.45 p.m., and at that time you will start with Mr. Laflamme.

AFTERNOON SITTING  
(Recorded by Electronic Apparatus)

TUESDAY, November 8, 1966.

● 3.57 p.m.

The CHAIRMAN: I will now call the meeting to order. Before recognizing Mr. Laflamme, I understand that Mr. Elderkin has certain information which we requested. If you would describe what it is, Mr. Elderkin, we will then distribute the information.

Mr. C. F. ELDERKIN (*Inspector General of Banks*): As requested, I would like to table exhibit number 15: Trust companies in Canada having directors who are also directors of chartered banks at March 1, 1966; exhibit number 16: Insurance companies in Canada having directors who are also directors of chartered banks at March 1, 1966; exhibit number 17: Loan companies in

Canada having directors who are also directors of chartered banks at March 1, 1966. Copies are available for all members of the Committee.

The CHAIRMAN: Miss Ballantyne, would you please have these distributed to members who are present, and also distributed to those not able to be present at this time?

Mr. Laflamme, you may proceed.

Mr. LAFLAMME: Mr. Paton, I would like to ask you this question: In removing the 6 per cent interest rate, how could it be possible to make more credit available to the public if the Bank of Canada does not provide more funds to chartered banks?

Mr. PATON: Mr. Laflamme, removal of the 6 per cent ceiling, in so far as the chartered banks are concerned, would not have any effect, *per se*, on the total money supply. It would greatly facilitate the banks' ability to compete for deposits in the pool of funds available, thereby enabling them to accommodate the loan demands which are made on them by their business customers across the country.

Mr. LAFLAMME: But is not the possibility of having the chartered banks compete more with the other financial institutions a process of making much more money available to the public?

Mr. PATON: No; that is a problem that is peculiar solely to the governor of the Bank of Canada. It is his decision whether or not more money is going to be made available, or less money made available, to the public, depending on his interpretation and his understanding of the needs of the country.

The removal of the 6 per cent ceiling would remove what the chartered banks consider a blight, or an inhibition, on their ability to perform a function for which they are primarily organized, namely to provide credit facilities for Canadian industry, Canadian commerce and the Canadian public.

Mr. LAFLAMME: Mr. Paton, in your brief, why do you oppose declaring your annual losses?

Mr. PATON: Our reasons for this have been enumerated on very regular occasions and frequently. We rest our case substantially on the opinions which have been expressed in prior revisions both by the Minister of Finance and the Inspector General—if I may have the liberty of mentioning him when he is sitting beside me—they have been subject to quotations, from previous revisions, in which they supported and substantiated the feeling that the disclosure of the operating losses year to year, plus the full disclosure of existing appropriations for losses, would be inimical to the best interests of the Canadian public.

Perhaps there are two main reasons. Banks are probably peculiar, more than any other industry in Canada, in that they are dependent on public confidence for the development of their operations, in their day-to-day transactions through their 5,700-odd branches across the country, plus off-shore branches.

The second reason, perhaps, is that the knowledge that the banks do have these reserves available for losses which may eventuate, due to changes in



conditions, or due to decline in the economic conditions in the country is important to their credit judgment. The problem of having these disclosed, might well inhibit us in taking credit risks which we consider normal risks under current day operations. If we were to assume that every appropriation, every loss that we incurred, would have to be tabled and be placed on the record—particularly in the event of an economic decline, when it could be that these losses could be quite substantial this could have a detrimental effect on our ability or our desire to take risks. Bank lending is a risk, if not a risky business.

Mr. LAFLAMME: Yes; but with your experience, and talking about the confidence of the public in the bank business, do you think that the banks, in having such large losses every year, would lose the confidence of the people if they knew about these losses?

Mr. PATON: No sir; I do not think the extent of the size of the losses that the chartered banks have suffered over the years would by themselves disturb this confidence. I think we must remember that we have been through some 20-odd years of reasonably good times, and there could be occasions when the situation might occur, where there could be substantial losses. The purpose of these reserves is to provide for the time when an extreme situation might well arise.

Mr. LAFLAMME: Could we have some information on the percentage of average losses suffered by banks in the last 5 years?

Mr. PATON: I think the Inspector General tabled that information.

Mr. LAFLAMME: Do we have that information from Mr. Elderkin, Mr. Chairman?

The CHAIRMAN: Was that part of one of the early exhibits that we have before us?

Mr. ELDERKIN: No; in my evidence I related the percentage loss in the last year, which was .291 per cent.

The CHAIRMAN: Of what?

Mr. ELDERKIN: Of the related loans. If you want the dollar volume, I am sorry but I do not have it here. But that is the percentage loss. If I can remember correctly, the percentage loss over a period of 25 years was .151 per cent; but that took in some very heavy recoveries after the depression in the 30's.

Mr. LAFLAMME: What percentage did you say?

Mr. ELDERKIN: The percentage was .151.

Mr. LAFLAMME: In reading your brief, I realized that you made a reference to the fact that the proposed legislation does not take coin into account when calculating your reserves. What is the percentage of coin that a bank would hold?

Mr. PATON: I might be corrected by some of my colleagues, but I think the amount of coin held by all the banks is roughly \$40 million.

Mr. LAFLAMME: In total?

Mr. PATON: Yes.

Mr. LAFLAMME: Within all the banks?

Mr. PATON: Yes; in the 8 chartered banks.

The CHAIRMAN: Mr. Laflamme, would you yield to Mr. Cameron for a few moments?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): How long do the banks hold the coinage. I was under the impression that they shipped it back very quickly.

Mr. PATON: Perhaps I should say that it is probably the most expensive money we have in our tills. There are some branches which have a surplus and there are other branches which have a deficit, depending on the nature of their business. Therefore, there have to be trans-shipments from one area to another; and this is done—I think I am correct in saying this—largely between banks. The Bank of Canada does supply silver when required, but the Bank of Canada is only in a limited number of areas, and all through the rest of the country there are transfers, in many cases between branches of the same bank and between branches of different banks. Transportation is expensive.

Mr. LAFLAMME: May I ask one other question, Mr. Chairman? Mr. Paton, I would like to know if you have any thoughts on the possibility of reducing the interest rate on guaranteed loans through having more power to compete with other financial institutions? I am speaking of guaranteed loans.

Mr. PATON: Loans guaranteed by the government of Canada?

Mr. LAFLAMME: Guaranteed by the banks—by the borrower.

Mr. PATON: Do you mean secured loans, sir?

Mr. LAFLAMME: Yes.

Mr. PATON: In a normal credit climate—and I think it is reasonable to say we are in an abnormal one now—it is common to have various rates on loans to an individual against which he hypothecates securities to obtain a preferential rate. At the present time this is not so, because we have one rate, with one or two exceptions, regarding government guaranteed loans. The rate to the public is 6 per cent, irrespective of the risk of the loan.

Mr. LAFLAMME: Yes; but when we look at the losses suffered over the last 25 years, you did not suffer many losses, or lose much money.

Mr. PATON: I think there might be confusion here, Mr. Laflamme. The rate that Mr. Elderkin gave us was an average of 25 years' losses. In recent years this has been somewhat higher than the average. When you translate these percentages into dollar amounts in relation to the total risk assets that we have it adds up to a fair amount from the dollar angle. Considering the narrow margin of profit within which the banks operate in relation to the very, very substantial assets they have, a very modest loss, percentage-wise, could have a very serious effect on any one year's income. We make this point in our brief, actually. We say: "Because of the overwhelming size of their liabilities and assets in relation to the income of any one year a very small percentage loss on assets—less than

1 per cent—would completely wipe out the year's income of any Canadian bank, producing an over-all net deficit”.

This is the problem area with the banks.

Mr. LAFLAMME: Thank you, Mr. Paton.

Mr. ADDISON: Mr. Paton, I would like to ask if the banking association is in favour of the near banks becoming banks under the Bank Act, in other words, taking exactly the same form as the chartered banks?

Mr. PATON: Perhaps, I could ask Mr. Coleman to answer that question, Mr. Addison. I will divide up the honours here, if I have your permission, Mr. Chairman.

Mr. ADDISON: Between Toronto and Montreal?

Mr. PATON: I am not deliberately ducking, there will be no question of judging the quality of the answers.

Mr. J. H. COLEMAN (*Vice-President, The Canadian Bankers' Association and Chief General Manager, The Royal Bank of Canada*): Mr. Addison, as I understand your question, you are asking if the banks would have any objection to near banks being chartered?

Mr. ADDISON: That is correct.

Mr. COLEMAN: The answer is no.

Mr. ADDISON: In the event that the near banks do not become banks in the sense of the chartered banks, will they have the opportunity of using the facilities of the clearing operations?

Mr. COLEMAN: Yes. Traditionally they have always had that, and there has never been one refused, to my knowledge.

Mr. ADDISON: Are there dues paid by the chartered banks to the banking association each year?

Mr. COLEMAN: Well, the expenses of the association are divided among the banks on a formula basis.

Mr. ADDISON: Would this cover, for example, the rewards for robbery and this sort of thing?

Mr. COLEMAN: Yes, any rewards paid by the bankers' association; but in some instances individual banks make rewards—or awards, I should say.

Mr. ADDISON: In so far as the depositors are concerned, is there a differential between what the chartered bank normally pays on deposits and what they lend at. In other words, is there a bracket in there that is similar in all banking operations, which covers overhead, profits and so on?

Mr. COLEMAN: No; I do not think there is; I do not think there is a constant margin. As was mentioned this morning, savings accounts attract a rate of 3 per cent. The banks do pay, and are paying, as high as 6 per cent for deposits of size, to get the money to be competitive. But the average margin has to exist for the



bank to make a profit; so what they lose on the potatoes they make up on the peanuts, or something like that.

Mr. ADDISON: We all recognize that the competition is not so much the question of the rate on the borrowed money; it is a question of getting the money. But, in so far as the banking institution is concerned their competition is for funds. The reason I asked the question about near banks is that the chartered banks have been at a disadvantage. Once the interest rate is allowed to float free, does this mean that the chartered banks will compete in the same manner as the near banks do at the present time?

Mr. COLEMAN: It is just for this reason that we would like to see the ceiling lifted—to enable us to compete on the same rules as those of the people who are competing with us.

Mr. ADDISON: Perhaps this is an anomaly—and we have a committee investigating this at the present time—but the near banks are offering premiums and prizes and so on and so forth to attract deposits. Does the banking association agree with this practice?

Mr. COLEMAN: We have not done it so far, therefore I would say that as of now we do not agree with it. We cannot afford it.

Mr. ADDISON: But this does not mean that you might not be in the coffee percolator business?

Mr. COLEMAN: This is quite possible.

Mr. ADDISON: Does the banking association have any objection to the individual banks disclosing their share interests in other companies, which are asked to be disposed of by 1972?

Mr. COLEMAN: Mr. Addison, I would say that this is a matter for the individual bank and not for the association.

Mr. ADDISON: Does the banking association have any objection to the ruling out of people who work for a government agency, or who are directors of Crown corporations, being directors of Canadian banks?

Mr. COLEMAN: I cannot think of one, and I cannot think of any objection, except that it seems to me that in the new, proposed legislation, in the case of a bank that is endeavouring to get a charter, there is a prohibition to that effect.

Mr. ADDISON: Well, in that particular bank; but in this bill it may be included as an amendment.

Mr. COLEMAN: Quite frankly, Mr. Addison, it is not something I had thought about. I cannot, offhand, think of a civil servant or an officer of a Crown company holding a directorship in a bank.

Mr. ADDISON: There is one now.

Mr. COLEMAN: There is one?

Mr. ADDISON: Dr. Keenleyside, I believe, in British Columbia.

Mr. PATON: He is a director of our bank, The Toronto-Dominion Bank. He is not a director of a federal Crown corporation.

Mr. ADDISON: No; I am speaking of a government agency, though.

Mr. Paton, you mentioned there was close co-operation with regard to chartered banks. The spirit of the bill, as outlined by the minister, is to increase competition, with which I am in full agreement. I am also in full agreement that the ceiling should be lifted. But they go hand in glove, and I think we, in this committee, must be assured that there will be free and equal competition.

Is it the policy of the chartered banks to discourage the hiring of personnel from each other?

Mr. PATON: No, Mr. Addison; there is no inter-agreement; there is no implied agreement. It is a fact there has not been much interchange of employees of our banks, certainly at the senior level. I suppose you could say that it is very, very seldom that such a thing happens. At the clerical level, from time to time there is a movement, perhaps, mainly in the female help, where there is a location problem—where the branch of another bank might be closer to the employee's home. There is an area there where there has been some interchanging in recent years—some movement. I could put it this way, that no bank sets out deliberately to attract staff members of another bank by offering them higher remuneration or better working conditions or a better looking manager or any such thing as that. But conversely there is no agreement against it.

Mr. ADDISON: The spirit of this bill is free competition, and the purpose of the Minister, obviously, is to bring this about, with a very minor penalty if it does not come about. Recently in the House the Minister of Energy and Resources read a letter of undertaking between the Trans Canada Pipe Lines and the Government where the penalty was \$1 million for each and every offence. Here we are speaking of \$5,000. I just have a feeling that perhaps close co-operation may not bring about the true spirit of competition. I am not thinking so much about lending as I am thinking, perhaps, so far as the depositor is concerned, where your service charges may be the same. There may be a 4½ per cent interest factor on savings accounts all across Canada. If the spirit of this bill is going to be successful then there must be clear competition between the banks and no written or unwritten agreements.

Mr. PATON: This, Mr. Addison, would create no problem so far as the banks are concerned. I do not think there is any doubt in my mind when I say there would be completely wide-open competition among the banks. There is at the present time.

This is not to say there would not be a similarity or identity in rates. It stands to reason, provided we have efficient operations and our costs are relatively the same, that we must, as an industry-wide operation, eventually end up with uniform rates. For example, if one bank was offering more for savings than another bank then very quickly this bank would be inundated with savings accounts, and vice versa. Of course, under the new act agreements would be barred, or any possibility of an agreement would be barred, under this section; but it is inevitable that lending rates and general rates on deposits will be certainly very close to identical except for this one thing, that if the banks are free to attract deposits they will have freedom to develop new sources, new forms of savings and be able to offer—I hope we always stop short of giving away percolators, etc.—real benefits in the form of interest rates in one shape or form, because there will be this keen competition to provide these.

Mr. ADDISON: I would just like to ask one other question, Mr. Chairman, of Mr. Paton.

Does the banking association have any type of voluntary inspection with regard to any particular bank, for example, becoming more deeply involved, say, in consumer lending than in carrying on a general banking business? I understand someone was talking about one bank where 32 per cent of their assets were tied up in consumer loans. Is there any policy, as far as the banking association is concerned, in this regard?

Mr. PATON: This would be completely outside the field of the association. Early this morning I gave a résumé of the functions of the association. This would be a question solely for the Inspector General. No individual bank, or group of banks, could be a governing factor. This is a management question. The management of any one bank would have to decide how it would deploy its assets, and would be subject to the inspection of the Inspector General whose responsibility it would be to take what action he thought necessary.

The CHAIRMAN: I propose to recognize Dr. McLean, Mr. Fulton and Mr. Grégoire, in that order.

Mr. McLEAN (*Charlotte*): Mr. Paton, I have a few general questions. It has been stressed that you need the ceiling lifted to compete. I suppose I am rather conservative that way but do you compete with such people as Atlantic Acceptance and Laurentide? Do you wish to compete with those people?

Mr. PATON: Dr. McLean, they do not come within the ambit of near-banks.

Mr. McLEAN (*Charlotte*): I was just asking a question about the kind of competition. It is just the near-banks with which you wish to compete?

Mr. PATON: That is correct.

Mr. McLEAN (*Charlotte*): If I was a banker I would not wish to compete with some of the near-banks, but I see no reason why the ceiling should not be taken off. Money is international and you must control it. I think that the United States at the present time is not doing very well in handling the situation. They are trying to get dollars back from Europe and they never succeed in raising the dollar rate in Europe. I think it is up around 8 per cent now. It seems to me that the competition now is the competition for money and not for loans. A while ago, I remember when it was competition for loans, but now it seems to be competition for money. As long as the Bank of Canada and the reserve banks in the United States are going to make the money scarce—and I believe the banks in Europe are going to make the money scarce—we are going to have this condition, are we not? It is a competition for money, and we are going to have that condition as long as the banks in the United States and the Bank of Canada are putting the screws on. The commercial banks cannot do anything about it, can they?

Mr. PATON: No; I would say this, that I would like to get back to that Utopian time when there was competition for loans. That would enable us to perform our function better and I would presuppose we were getting deposits in to enable us to make these loans. I agree with you that the current situation which we are discussing is international.



Mr. McLEAN (*Charlotte*): Keeping the lid on in Canada is not going to help the situation as long as money flows out of Canada, flows into Canada, flows from the United States to Europe and flows from Europe to the United States. The ceiling in Canada is not going to have much to do with it, is it? You have to pay what everybody else is paying.

Mr. PATON: Perhaps are you confusing the Euro-dollar question and the domestic question?

Mr. McLEAN (*Charlotte*): It enters into the picture.

Mr. PATON: Yes; but our concern on the 6 per cent is confined basically to our situation in respect of the financing of Canada's economy.

Mr. McLEAN (*Charlotte*): Well the 6 per cent ceiling in the banks, I would think, would tend to hold down borrowing in Canada to a certain extent. I can remember when we borrowed in New York because the rate was lower there than in Canada. If you are doing an international business you borrow where you can borrow the cheapest. It seems to me that by keeping the ceiling on here we are not helping the situation at all.

I would like to ask about your debenture financing. It seems that the banks in the United States have gone into that. Why should you go into debenture financing and not capital expansion?

Mr. PATON: Actually, it is a question of cost, Dr. McLean. The debenture financing, on the basis proposed in the act, provides us with the legal power to issue debentures on a limited, prescribed basis subordinated to our deposit liabilities, and thereby they would be free of cash reserves. The interest would be in pre-tax expense of the banks' operations, and to go the capital route could be more expensive.

Mr. McLEAN (*Charlotte*): If you borrowed at 6 per cent and you were in the 50 per cent tax bracket I suppose you could charge so much to the government.

Mr. PATON: Debentures at 6 per cent?

Mr. McLEAN (*Charlotte*): Yes.

Mr. PATON: The interest on such debentures would be a pre-tax cost.

Mr. McLEAN (*Charlotte*): If you had capital expansion you would have to pay the full rate on it.

Mr. PATON: The dividend on our equity shares would be after tax.

Mr. McLEAN (*Charlotte*): There has not been much said about the banks' shareholders. Could you tell us the shareholdings held in the 8 chartered banks in Canada.

Mr. PATON: There are 118,000 shareholders of which some 90 per cent are registered as having addresses in Canada.

Mr. McLEAN (*Charlotte*): There are 118,000 shareholders?

Mr. PATON: I have the figures somewhere, if you will just give me a moment. Dr. McLean, the total shareholders in October, 1965, the fiscal year end, was 118,413.

Mr. McLEAN (*Charlotte*): What percentage would be Canadian?

Mr. PATON: The Canadian-owned was 104,000 or 88.16 per cent.

Mr. McLEAN (*Charlotte*): What percentage would be held by any one company or individual?

Mr. PATON: That information is not generally available, but each bank provides the Minister, through the Inspector General annually, with a list of the shareholders of each bank in excess of 500 shares.

Mr. McLEAN (*Charlotte*): What I was trying to get at is that the banks are principally owned in Canada and they are principally run by the management. Back in my day—the day of Sir Herbert Holt and those people—they seemed to run the bank, but it seems to me that today they are run by management for the shareholders.

Mr. PATON: Dr. McLean, we do not even have as many men of a certain ethnic origin in the management group as we used to have.

Mr. McLEAN (*Charlotte*): Well, with lending, the risk and the rate really are tied up together. Is that correct?

Mr. PATON: In the lending?

Mr. McLEAN (*Charlotte*): Yes.

Mr. PATON: Yes, sir. Under normal conditions this is the way it should be.

Mr. McLEAN (*Charlotte*): But you cannot relate the risks to the rate when you have a ceiling of 6 per cent.

Mr. PATON: Exactly.

Mr. McLEAN (*Charlotte*): The Bank of Canada do a great deal of banking abroad. Are the inner reserves related in any way to the banking business they do abroad to cover any risks that you take in your business outside of Canada.

Mr. PATON: These would constitute part of the risk assets.

Mr. McLEAN (*Charlotte*): I remember one time a great many years ago when the Bank of Montreal lost a great deal of money in Mexico. So, it really is essential that you have something to come and go on when you are doing business abroad, and you do not know when something is going to happen in a foreign country, say, like the Dominican Republic.

Mr. PATON: I have just been corrected. In that statement I made in connection with our reserves the eligible assets are Canadian assets.

Mr. McLEAN (*Charlotte*): You cannot use them for any losses abroad?

Mr. PATON: Mr. Elderkin, can you confirm that.

Mr. ELDERKIN: I am sorry, I did not hear the first part.

Mr. PATON: The eligible assets for our reserves are confined to Canadian assets?

Mr. ELDERKIN: No. The eligible assets so far as loans are concerned, may be here and abroad, but a great many loans are not eligible loans. I might say that the whole thing is spelled out in Exhibit No. 14, which was tabled.

Mr. McLEAN (*Charlotte*): About the inner reserves?

Mr. ELDERKIN: That is correct. I have the assets on which they are based.

Mr. McLEAN (*Charlotte*): They cannot be used for losses abroad outside Canada?

Mr. ELDERKIN: Yes. If you will look at Exhibit No. 14, Mr. McLean, you will see it there.

Mr. McLEAN (*Charlotte*): Banks are more or less protected in that, as I think they should be.

Mr. PATON: My original answer then was more right than my correction.

Mr. McLEAN (*Charlotte*): It was brought out about the companies holding so much in their current accounts. It is quite true that companies often have \$100,000 outstanding, but there are cheques outstanding against that; and while they have a compensating balance there are really cheques out against that compensating balance. So it is not doing any harm to the company, say, to keep \$100,000 on deposit because there are cheques outstanding against it all the time. I know that a couple of the big companies in Canada here make up their balance sheet and show \$800,000 or \$900,000 in cash on one side and, on the other side, they show outstanding cheques—so, if they were to put one against the other they would be entirely wiped out. But that \$800,000 or \$900,000 would be in the bank at the same time, so this compensating balance, really, in a great many cases, does not mean anything to the company that has the compensating balance there.

I think that is all that I wanted to ask at the present time.

The VICE-CHAIRMAN: Thank you, Mr. McLean. Now we will call upon Mr. Fulton.

Mr. FULTON: My questions probably will take about half an hour so I will not mind if you interrupt me at any stage. I would like to come back on the second round.

Mr. Chairman, first I would like to ask Mr. Paton a question that I had intended to ask Mr. Rasminsky but I did not have time before he left. I would like to check it again with Mr. Rasminsky when he comes back. My understanding is that the Bank of Canada's management of monetary policy is done largely by the control of the reserves of the deposits of the chartered banks with the Bank of Canada; that is to say, under this new legislation, if they want to restrict credit they will call up secondary reserves, thus restricting the lending capacity of the chartered banks. That is my rough understanding of the situation. I wonder, in addition to the mechanics of control, whether the informal discussions, which you referred to this morning, that the chartered banks or your association has with the Bank of Canada, embrace discussions of a type of lending activity that the Bank of Canada thinks the chartered banks should continue in or withdraw from time to time, the object, perhaps, being to suggest to the banks that they restrict loans to the type that they feel or it is felt will expand production, and from time to time that you withdraw from the consumer lending field, or other suggestions the Bank of Canada might think were appropriate to make with respect to overall monetary policy and credit supply. Does the Bank of Canada have that kind of discussion with you as to lending and credit policy, or is its influence on the chartered banks confined simply to its regulation of the reserves?



Mr. PATON: The major influence the Bank of Canada has on the chartered banks, Mr. Fulton, is undoubtedly through its operation of their cash reserves but, as we mentioned this morning—and you referred to it—we have very frequent and regular informal discussions with the governor. These discussions range quite far and wide across the whole ambit of the general economy. An indication perhaps is a most recent subject that was of prime importance as the result of the United States guidelines, if it were felt that there might be pressure on the Canadian banking system to finance subsidiaries of United States or other foreign companies for requirements that formerly or otherwise might have been supplied by the parent company. This discussion veered around the fact that it must be very essential that, by virtue of the banks' endeavouring to satisfy these new requirements that might come from the guide lines this would not be done at the expense of the Canadian-owned and controlled corporation, possibly of a smaller size, who had a complete inability of going elsewhere to obtain its financing. This is the area of discussion which takes place with the governor of the bank.

If it is felt, perhaps, that there is a somewhat untoward expansion of the general total in consumer credit in relation to the general economy, there might be a discussion along the lines that it might be well to slow down our participation in this type of financing.

This is the area that we discuss. Close attention is paid by the chartered banks, to the Bank of Canada's feelings in this respect and, within the confines of their own management choices and dictates, they endeavour to co-operate as much as they can.

Mr. FULTON: It would be correct to say, then, that the Bank of Canada—and I am not saying this as a criticism; I am only asking if I am correct in stating it as a fact—in addition to its technical or mechanical control of the credit system through the reserve operation does, by discussion, at least expect that it will influence general banking policy in terms of the direction in which lending activity should follow?

Mr. PATON: I would agree with that, except that I would not want to leave the impression with the Committee that they have such an impact that it would change the line along which individual banks would want to go. We still want to operate our own banks.

I would also say that there is a remarkable uniformity between the trend in which we would like to go and the governor of the bank, and this does not necessarily initiate with the governor—I mean the suggestion does not come from him originally. We have found that we have a very common meeting ground in the discussions we have had with the governor. So there is an impact, yes, but not such an impact that there is an implication that here is a laid-down instruction we must follow.

Mr. ADDISON: Mr. Chairman, could I ask a supplementary question? Mr. Paton, you say this was left up to the banks entirely. Regarding the distribution of the available money you have to lend, to the consumer and other categories—you are in charge of the Bankers' Association—would you say that this is similar in each bank? In other words, is the amount of money going into consumer credit items, for example, proportionately the same in each bank?

Mr. PATON: No, Mr. Addison. There is actually a wide variance in the percentages of investment by each bank in certain areas. You might find that one bank is substantially higher in the textile industry. You might find that another bank is higher in the construction industry. There is no uniform percentage.

I think each bank is well aware of where they are relatively heavy in any one industry—and when I say “heavy”, I mean taking their total assets in relation to the total banking assets. If a bank had 10 per cent of the total banking assets and had 20 per cent in one industry, then they would know that their investment there would be greater than the average.

Mr. ADDISON: Is there not a danger that the banking institutions will go to the areas of the higher profit, which is the consumer field, thereby restricting money available for small businesses, for example, at relatively lower rates?

Mr. PATON: There is a possibility but I do not think that there is any danger. The banks' performance over the years—and when I say “banks” I mean all of the banks—I think has definitely indicated this. The very fact that we have the banking system we have, where we have gone into areas where it undoubtedly was expensive to go and it took quite some years before we got on to a paying basis, is indicative of this. Our desire is to serve the whole country and the whole economy, and we consider this consumer finance area an area in which we are justifiably in. But I do not think that there is any danger—speaking of the banks as a group—of this affecting the banks' judgment, merely through the fact that this is, perhaps, a higher revenue producing area in which to lend.

Mr. FULTON: It would not be an unexpected line of discussion on the part of the banks for you to hear suggestions coming from the Bank of Canada that, for instance, under present circumstances and for a limited time, the banks might consider restricting their loans for consumer purposes and concentrating or emphasizing loans for what I might call productive purposes. Would that be the kind of suggestion that might come?

Mr. PATON: Very rarely, Mr. Fulton. I would say that if it did happen it would happen very, very rarely, and only because of a very serious situation arising. We have not had that specific direction, to my knowledge. There was a time some years ago when we did cease expanding our lines to the consumer finance group of companies—I think, perhaps, you have that in mind—when we more or less corrected a situation that existed at that time where it was common practice in the consumer financing field to have substantial lines of credit. The availment of these lines was at a relatively low ebb, and in one of the tight money eras that we have had over the last fifteen years, we did limit the usage of these lines of credit to the actual peak amount that they had previously used.

I would just like to supplement my answer to Mr. Addison's question, because I would not wish to feel that the consumer finance business is so substantially more profitable than the ordinary lending. The administration costs are quite a bit higher in that form of lending than in ordinary straight-forward lending.

Mr. FULTON: To turn to a topic somewhat related to what I was discussing with you initially, Mr. Rasminsky expressed the opinion in his evidence that the purposes of the Bank of Canada's function of controlling monetary policy—the legislation and the system as it is and as it will exist when this bill goes

through—was adequate. I was asking him a question in the context of our discussion about some sort of federal control of the non-bank financial institutions, and he said he felt that for the bank's primary purpose of control of monetary policy he had adequate resources in his hand. Would you have any comment on that? Also, in answering a further question of mine, he admitted that that might require review, say, in the next ten-year period, in the light of the possible further growth of the activities of the non-bank financial institutions, but that he felt for the next 10 years this would be adequate for monetary control purposes.

Mr. PATON: I think I would be expressing the feeling of the association, Mr. Fulton, if I said that perhaps we do not quite agree with the Governor as to the length of time that this will not be a concern. He is better able to assess the problem than we are, but with the rapid growth of the near-banks' assets that has taken place—and these figures were tabled during the last two weeks while Mr. Rasminsky was here—it seems to me there will be a continuation of such a growth. Perhaps it is not entirely reasonable to expect this will take place, nevertheless, on the information we have at hand and perhaps the superficial knowledge that we have, we think that there is a possible hindrance to the global control of the money supply. Although perhaps this is more of a layman's suggestion, it seems to me that in any case, from a point of equity, where you have two people feeding out of the same trough, you can manipulate them much better if you have control over the whole package.

Mr. FULTON: Would it follow from that last portion of your answer, that the expansion of these other institutions are an influence in the field and are not actually under the control, that for the Bank of Canada's measures to be effective—they have been confined to the chartered banks—they might have to be a little more extreme in terms of the chartered banks, and their effects on them than if the whole section was control. Does that follow?

Mr. PATON: Yes, it does in my opinion. To achieve the goal that the governor wishes, the impact on the banks is larger than if the overall group were under his control.

Mr. FULTON: Then, could I lead from that to the area of the mechanism of control, the reserves that the chartered banks are required to keep with the Bank of Canada. On pages 9 and 10 of your principal submission you discussed it. I think from the comments you make there that it is the view of the Bankers' Association that the secondary reserve requirement is not necessary and they work unnecessary hardship.

Mr. PATON: Yes, that is correct. The Association feels that the statutory secondary reserve is not necessary.

Mr. FULTON: Do you mean by that, not necessary to ensure liquidity, and soundness of the banking system or not necessary for the exercise of effective control of monetary policy—or both?

Mr. PATON: In going back perhaps to the origin of the secondary reserves that we currently have been keeping—and this was by agreement with the Governor of the Bank—this was instituted maybe eight or ten years ago, at the time of a need, perhaps, at the time of a credit crisis situation in 1956. That was done by agreement between the then Governor and the chartered banks.



The crisis situation expired and we got back to a normal situation again, but the secondary reserve did not disappear; it remained. So, we have grown accustomed to a secondary reserve over the last ten years.

In our brief to the Porter Commission we recommended strongly against putting it in statutory form, and suggested that it was not necessary for the effective monetary control needed by the Bank of Canada.

I may be contradicting to some extent the Governor's evidence that he gave last week. I think he put it that the Porter Commission was non-enthusiastic about it. I would prefer to take a little stronger approach and say that the Porter Commission could not see the need for it and tacitly, at least, implied that this was not something that in their opinion was required. Therefore, we are still of the opinion that having it as a statutory requirement is not necessary, certainly from the view point of liquidity of the banks, because management of the banks are well aware of what they need to look after their liquidity problems. The secondary reserve must be, as you know invested in day to day loans and Treasury bills. These are currently yielding what at certain times would be regarded as a very adequate rate of interest. Nevertheless, no matter what the level of interest rates are, Treasury bills are a relatively low yielding asset.

Mr. FULTON: Do I understand you to say that the primary reserve is subject perhaps to some minor differences of opinion about what is justified on the basis of ensuring liquidity? I raised, earlier with Mr. Rasminsky, the question of interest on the reserves held by the chartered banks with the Bank of Canada and he felt, as I recall it, that if the Bank of Canada was required or allowed to pay interest to the chartered banks it would reduce the effectiveness—that is the interpretation I put on it—of the Bank's ability to exercise control of monetary policy.

It occurred to me, therefore, that one might perhaps, while not quarrelling with Mr. Rasminsky, put the proposition—and I would like to obtain your comment on it—that in so far as the reserves, which are held by the Bank of Canada under the primary section, correspond roughly to the insurance of liquidity, then probably the chartered banks should not get interest on that; but if the Bank of Canada calls upon the chartered banks to build up reserves substantially in excess of that for Bank of Canada policy purposes, it might be fair to suggest that some interest at any rate be paid to the chartered banks on those reserves while they are there. Would that seem to you to be equitable?

Mr. PATON: Yes, I would say this would be equitable—we recognize that perhaps it is not—I was going to say feasible, but I think that is too strong a word. There is an area in which—and that area might be 5 per cent—we would require to hold for the normal operation of our day functions, which includes Bank of Canada notes and, we hope, coin eventually; anything over that is a penalty to the chartered banks. I think in some countries interest is paid by the federal reserve bank and by the central bank. It is a subject that we have been cognizant of, Mr. Fulton, but it is not one that we have made a strong plea for to date in any of our deliberations. It is tied in perhaps, to a very large extent, to the cost of handling government business, at a very substantial cost to the banks. I think there is a case of equity that could be made out for payment of some form of interest on some part of the balances which the Canadian banks hold with the Bank of Canada.

I have a note here that Australia pays  $\frac{3}{4}$  of one per cent and Italy and India are two other countries that pay interest on these.

Mr. FULTON: Moving next to the question of the prime basis upon which the calculation of these reserves is now required to be carried out, or will be, moving from a one month average to a fortnightly average, I understand, when the calculations are finished, that if you are below the reserve percentage which you should have had there, then the banks pay a penalty. Suppose the figure for this month should have been 8 per cent and you have 7.98 per cent, which is fairly close in percentage points but it may be a large amount of dollars when you apply it to what should have been there, do you have to pay a penalty on that deficiency?

Mr. PATON: We always reach the minimum 8 per cent. The Bank of Canada provides a line of credit for each bank, and on application by an individual bank they can borrow from the Bank of Canada against security of government of Canada bonds. This is at the prescribed Bank of Canada rate. Now, if toward the end of the month it is necessary to go to the Bank of Canada a second time to ensure that we meet the average 8 per cent—

The CHAIRMAN: You are referring to what section, sir?

Mr. PATON: Clause 72.

The CHAIRMAN: Clause 72? It is clause 141: Failure to maintain reserves, at the top of page 96 in the English text.

Mr. PATON: I was going on the basis that this never happens—"...Knowingly fails to maintain a cash or secondary reserve..." In my experience, anyway, it has not happened. There is a penalty when we have to go back to the Bank of Canada more frequently than once per month to borrow money.

Mr. FULTON: To borrow money.

Mr. PATON: There is a penalty rate that the Bank of Canada will charge, and this clause 141 deals with the failure to meet the requirements of clause 72.

Mr. FULTON: Do I understand you to say then that unless it can be shown that you did that deliberately, you do not pay a penalty or if at the end of the calculation period, there was a deficiency, unless it can be established that that was done deliberately by the bank, the bank would not have to pay a penalty? I do not understand it. I thought you would have to pay the penalty if there was a deficiency, period.

Mr. PATON: This is a subject on which I perhaps might ask my associate, Mr. Hackett, to speak, Mr. Fulton, because in my own personal experience I have not been faced with this particular problem of where a bank knowingly fails to meet this requirement. I would assume that if there was this deficiency that it could not be anything else but done knowingly. Otherwise, it is quite a reflection on one's ability to manage one's bank. Mr. Hackett, would you mind answering this question.

Mr. FULTON: I wanted to come back to the discussion of the equity or otherwise of the narrowing of the period of calculation to two weeks or a fortnight. My question was, am I right in understanding that if at the end of the present system, when the calculation must be made, it was found that you had

instead of the required 8 per cent only 7.98 per cent, and you have been deficient .02 per cent, the bank in question would have to pay a penalty on that deficiency?

Mr. W. T. G. HACKETT (*General Manager (Investments), Bank of Montreal*): The act provides that the deficiency is then deemed to be a deficiency for the full month and the penalty is assessed at the rate of 10 per cent per annum on such deficiency, calculated on the assumption that it is in effect for the full month.

Mr. FULTON: Yes.

The CHAIRMAN: Mr. Fulton, up to now you have had approximately 25 minutes, allowing time for some of the supplementaries, and perhaps you would ask just one or two more questions at this time. You might wish to keep the balance of your questions for the next time.

Mr. FULTON: Thank you, I will. Mr. Hackett, while I have the greatest respect for the bank's ability to know from time to time how much reserve it should maintain, but if you narrow the period now from a month to two weeks, would the chance of error with the two week period be more substantial than the chance of error with a one month period?

Mr. HACKETT: I would answer that question this way, Mr. Fulton that in the management of cash the banks are endeavouring, and indeed it serves the purposes of the Bank of Canada for them to endeavour, to work as closely to the prescribed 8 per cent average ratio as they can. Such an operation inevitably involves a certain amount of guesswork and, speaking for myself perhaps, a certain amount of good luck from time to time—and, inevitably, there is also the occasional bad guess. One has to assess the effects on your position of trailing gains or losses from day to day on the basis of information that is always incomplete, and we never quite know what the factors are arising outside our own control that are going to affect us.

Conceptually, it would be possible for a bank to get itself in a position where it approached the end of the monthly period on the present basis and found itself short and subject to the penalty, except for the fact that so long as the deficiency is within its line of credit with the Bank of Canada, it could always go and borrow it. Something would have to go very wrong on that. You would have to make one or two bad guesses, but it could occur.

When we come to the matter of shortening the averaging period, cutting it in half, I think it becomes a matter of mathematics, shall I say, where the element of guesswork or risk, the element of uncertainty, in providing for day to day swings and attempting to offset those swings is exactly doubled. Perhaps I can put it this way, that in a month any bank is going to have certain unforeseen clearing gains, it is going to have some unforeseen clearing losses. It can go through a bad patch for perhaps one, two or three days when the tide is running against it, but over the month you have a fairly good chance that the swings are going to average out, one against the other. The law of large numbers seems to work in this context to a considerable degree. When you cut the averaging period in half, you are just taking a double chance with every situation that faces you, a chance of perhaps having too high a reserve or a chance of having too low a cash reserve.



It also leads you into a situation like this. A bank may have a sizeable clearing loss, and it may have known of this clearing loss. In any event, it had it on, shall we say, the last day before the end of the first fortnightly averaging period of the last day of the averaging period. It may know very well that two days afterward there is some transaction that they know of which will reverse this situation. Because of the change in the averaging base, however, the bank concerned may well have to take rather drastic action by way of calling loans in the day to day market or offering Treasury bills for sale and driving the price of the bills down and the market interest rate on them up. What I am trying to say, sir, is that it may have to hand a decided shock to the short term money market for a reason that would not be necessary at all if the averaging period maintained for the full month. I should add perhaps that at that point the situation becomes one of rather wider import than a matter affecting the banks and the Bank of Canada, because what you have to do unnecessarily in this context has certain market effects. It may make short term borrowing temporarily more expensive for other short term borrowers.

Mr. FULTON: I have one final point in this field and then I will stop. If it is the desire that the averaging period be narrowed, presumably for the purpose of making performance follow more closely to trends. Would it be equally effective if the principle was that the bank must maintain, for the next two week period, a reserve based upon performance on the preceding two week period.

Mr. HACKETT: I think I see your point, Mr. Fulton. I can perhaps get at it this way: in the present system, as I say, each bank endeavours to work as close to this 8 per cent average as is possible. In point of fact, a very good job is done; the average monthly runs around, I would say, 8.09 or 8.10 which is a pretty characteristic average. As a matter of fact in 1965, the characteristic average was 8.10. It was the same in 1964 and I think it has been a little less in 1966. Any bank—well perhaps I should not talk about any bank—I will talk about the bank I have the honour to serve—I would personally regard an average of 8.20 as a bit of a moral defeat, something would have to have gone awfully wrong. But the point is this, that if I have a cash ratio of say 8.15 in the month of November that average does not carry over into December. When we get to December we rule it out and begin all over again. I take your point, Mr. Fulton, to mean that in this two weeks or this fortnightly averaging context, it would ease the situation, if the bank were allowed to carry over into the second period, and obtain the benefit of any surplus that it might build up in the first period. That might alleviate the situation somewhat, but the other thing would obtain, also; you would have to carry forward any deficiency you might have. I would think that one would get a better and smoother result if the averaging period were left on the monthly basis, as it is now.

Mr. FULTON: What you have told us then is that you anticipate, on the basis of your experience in this field, that the halving of the average period may compel banks to take more drastic action market-wise than if it was left to the market.

Mr. HACKETT: On the basis of my experience in this field, and I am sure it is the experience of others in the banks who work in this same area, I think we

come down to a difference of opinion really. We are fully in agreement with the Bank of Canada's objective, which is to get quick, smooth responses on the part of the banks to the impulses generated by the central bank. There is no argument about that; that is not at issue. Where I think our view differs—this may be the kind of difference of opinion that arises when you are working in an area where you are in daily contact with and cognizant of the problems involved—is that our view is that this change will have rather the opposite effect to that anticipated by the central bank. We base that on the feeling that the element of uncertainty will be increased to such an extent that there will be rather a premium on playing a little more cozy, not taking quite as many chances as we can take when we have the whole month to average out.

There is one other very important point that I think should be introduced here. Up to now I think we have been assuming in this discussion that a bank can, assuming that its judgment is right and that its guesses are right, in point of fact, can actually do the kind of things that it would wish to do to smooth out a cash bulge in the market at the time it wants to do it and in the amount it wishes to do it. Unfortunately, our short term market is not all that receptive and is not all that sensitive. There are quite frequently, on the basis of my own experience, times when we have had money we wished to employ for the purpose of smoothing out our average, and it was just not possible, on that day, to employ it in the amounts that we wished, because the initiative is not wholly in our own hands. We can offer the money to the market, but for the operation to be complete there has to be a dealer or dealers who wish to borrow that money.

The CHAIRMAN: Perhaps I might assist the Committee by informing it that the bankers' association have prepared a paper entitled "Cash Ratio Management Proposed Twice Monthly Averaging Techniques," which I imagine expands on the concepts you have been putting forward.

Mr. HACKETT: I am aware of that paper.

The CHAIRMAN: Mr. Paton has brought it to my attention. I am not mentioning it to restrict your own very useful comments, sir, but merely to suggest that perhaps you might distribute this to the Committee. This might permit us, as we continue our examination of your group, to have a better understanding of your point of view. With that in mind I would ask the clerk to take that in hand.

Now if you have finished your initial questioning at this point, I would like to recognize Mr. Grégoire.

Mr. HACKETT: Perhaps, Mr. Chairman, the Committee might like to come back to us with some further questions.

The CHAIRMAN: That is why I thought this paper would be useful. It would give them an opportunity to look at it to supplement their understanding of what they have gained from your own comments.

Mr. HACKETT: Thank you.

(Translation)

Mr. GRÉGOIRE: In the Statistical Summary of the Bank of Canada for October 1966, page 258, there is reference to the Bank of Canada having bank

bills in circulation in the total amount of 2 billion 598 millions. So I suppose we can take it for granted that we have in circulation bank bills of the Bank of Canada for about 2½ billions.

Elsewhere, at page 662 of the same issue, there is reference to the fact that the chartered banks made loans to the amount of \$19,081,000,000, in short term securities, Treasury Bonds, securities issued or guaranteed by the government of Canada, such loans being made through agents or brokers to provinces, municipalities, grain dealers, finance companies etc., in the form of purchase of savings bonds, general loans, mortgage loans and the like. The total amount, then, was \$19.81 million. Can you explain the difference between the amount of bills in circulation and this difference of approximately 16 billion? I would like to know where the banks get these 16 billion to be lent whereas we have no more than 2.5 billion in circulation? This can be seen from the Statistical Summary itself.

(English)

Mr. PATON: Mr. Grégoire, in anticipation that I would be getting out of my depth here sooner or later today, perhaps it has been sooner than I thought, I have with me Mr. Bob MacIntosh, who is Joint General Manager of the Bank of Nova Scotia. With your Chairman's permission, I would like to direct your questions to him. Perhaps he will be able to answer more profitably than I.

The CHAIRMAN: Mr. MacIntosh would you like to proceed?

Mr. R. M. MACINTOSH (*Joint General Manager, Bank of Nova Scotia*): Mr. Chairman, if I could take a minute to review the question of the nature of credit expansion in the Canadian banking system, I hope I will perhaps be able to deal with it in such a way that I will not offend the sensibilities of my colleagues here and at the same time meet the interest of the Committee in trying to settle this question definitely for the purposes of these meetings. We will then, perhaps, be able to conclude the subject to your satisfaction.

I might say that for some years I used to teach the theory of credit expansion and I have practised it in the way that Mr. Hackett has recently been describing it, for a good many more years. There is no difference between the theory and the practice of banking and I think the theory and practice are well understood, not only in Canada, but elsewhere. In fact, I think it would be correct to say that the nature of the credit expansion system in Canada is no different from that which has obtained in many countries for a good many years.

The present central banking system and the nature of the commercial and near banking system, in Canada have existed, for instance, in the United Kingdom for over 100 years; in France and in the United States into the last century. At the present time there are more than 100 countries in the world with central banking systems which are not different in essentials from the Canadian banking system and financial system.

I want to make this point, Mr. Grégoire, because there is no sense in which the Canadian banking system is unique or different or magical in any way from the central banking systems of every other country which are well understood.



The process of credit expansion which takes place in the Canadian banking system, begins with the operations of the central bank. In deciding how much the money supply should be, the central bank takes account, as the Governor of the central bank described last week, of the credit conditions. Credit conditions in a term which encompasses not only the level of interest rate in the economy and the structure of interest rate of all kinds, but also the amount of deposits in the banking system, the amount of the note circulation and the amount of the deposits of the near banking institutions. All this has to be taken in account as well, of course, as our foreign exchange position.

In deciding to expand the volume of credit in the system, the central bank must take into account the conditions in the economy, the rate of growth of the economy and our external balance. If the gross national product is increasing for a variety of reasons by a rate of, shall we say, 8 per cent per annum, then other things being equal, the central bank may feel that it is appropriate to see that the amount of credit in the system is expanded by approximately 8 per cent also which would mean that ordinarily the level of prices in the economy would not change but that the amount of growth in business—may I finish Mr. Grégoire?

Mr. GRÉGOIRE: On a point of order, Mr. Chairman, this is not an answer to the question I asked. I already know all that which Mr. MacIntosh is saying and that is why I did not ask that question. He is not answering the question I asked. I have 20 minutes and I would like to be able to have an answer.

The CHAIRMAN: If I may deal with the point you have raised, I do not think any member can expect to automatically get the answer he would prefer or like from any witness. When he asks a question, he must, to some extent, bear the consequences of having asked it.

Mr. MACINTOSH: Mr. Chairman, that sounded like an infliction, but if I may continue—

Mr. GRÉGOIRE: I am very much against this, Mr. Chairman, but—

The CHAIRMAN: If I may continue to deal with the point you raised. In allotting to members and others participating in the work of the Committee the time for posing questions, I try to take into account such factors as the length of replies, supplementaries and so on. So that if Mr. MacIntosh, in trying to sincerely give us the benefit of his views in answering your question, goes on for a certain length then your period of time for asking questions will not thereby be reduced. The witness can be advised to continue and to say that he is entitled to answer this question in the way that he feels, for the moment anyway, is the best way he can do so.

Would you proceed, Mr. MacIntosh.

Mr. MACINTOSH: Thank you, Mr. Chariman. I do not wish to take an undue amount of time of the Committee and certainly not of Mr. Grégoire's time, but I would like, if possible, to deal with this in a manner which will, I hope, settle it, as I said before, for the purposes of this meeting.

The CHAIRMAN: Do not tempt fate.

Mr. MACINTOSH: I will keep that in mind, Mr. Chairman.

I was mentioning that the process of credit expansion being with the views of the central bank of the amount of credit which it considers to be appropriate to the needs of the economy. Having made a judgment which might involve, shall we say, a rate of expansion in the supply of money by 8 per cent per annum, it will then take certain actions in its own balance sheet which attempt to bring about those effects. But those effects are quite beyond the control of the Chartered banks. This is a matter which is within the unilateral power of the central bank to control. It is not our power. The chartered banks are not in the position to pull themselves up by their own boot straps.

Nor indeed are they unique in their ability to make loans. The Governor of the Bank of Canada described at some length the similarities between the nature of the chartered banks and the nature of the near banks. We would wholly subscribe to the remarks which he made the other evening and draw your attention to the tables which he presented to the Committee in this regard.

The central bank ordinarily carries out the process of credit expansion by open market operations, which is to say that it enters the open securities market and it buys securities. In the process of buying securities, it writes cheques on itself which become deposited by the seller for securities in a commercial bank. The commercial bank then deposits the proceeds of that cheque at the central bank and thereby increases its cash reserves.

If there were only one bank in the whole system and no other banks or near banks, then that bank having acquired cash would be in a position to make loans with the money it had so acquired. In theory it could lend all the money and the borrower could choose to take the money out in cash. The general manager could run down to the teller and ask if there is enough cash in the till to make the loan. This is not ordinarily the way we work.

An hon. MEMBER: I hope not.

Mr. MACINTOSH: What happens is that one bank in the system, having made a loan to an individual, that individual could spend the money, the money would end up in the hands of another person who would then deposit it back in the same bank because by definition there would only be, as I said, one bank, in this assumption. Therefore, the deposits of that banking institution would be recovered. It would acquire further deposits and it would make another loan, and so long as it was the only bank able, therefore, to hold the deposits, it would be able to continue to expand loans as its deposits increased.

However, that is a highly theoretical concept where there is only one bank and, in fact, there are eight chartered banks and a good many other near banks in the system. Therefore, the initial process of making a loan and giving a deposit to a customer does not lead necessarily to an expansion of that individual bank. The deposits may be drawn off by another bank which is a question of open competition. Therefore, the chartered banks individually and as a whole are not in a position to create in any sense the deposits which are on their books. They are government by the conditions which are made for them by the central bank and the system, as I say, which I am describing encompasses not only the

chartered banks but as the governor said, the near banks and there is nothing unique or strange about the system; this is the way it works.

Mr. GRÉGOIRE: Well, sir, may I ask my question now?

The CHAIRMAN: Do you want the same answer?

Mr. GRÉGOIRE: As I said, maybe it was a consolation which was no good. Maybe that is the fault.

As I said, the statistical summary of the Bank of Canada mentioned that there are notes in circulation from the Bank of Canada for \$2.5 billion and the chartered banks, according to the same summary of the Bank of Canada on page 662, have made loans for \$19 billion, making a difference of \$16.5 billion. Where did the chartered banks get the difference so they could lend it? That is the question for which I would like an answer.

The CHAIRMAN: Do you feel you can add anything to your previous answer?

Mr. MACINTOSH: No, I do not, sir. I understood the question originally in French and I understand it now in English but my answer is the same.

Mr. GRÉGOIRE: We should know where they get the difference in order to lend it.

*(Translation)*

I will give another example. I have here a newsletter from the Royal Bank of Canada,—I think we have the General Manager of the Royal Bank here—where the answer is given. I would like to get some additional information on this, if you will allow me, Mr. Chairman. Before I quote from this newsletter published in June 1966,—there is also the English copy here, which is headed Economic Trends and Topics, June, 1966,—I might say I wrote all the Presidents of the chartered banks, to the Minister of Finance, and to the Governor of the Bank of Canada. May I ask now whether you are ready to endorse what is set out in this newsletter, if your views are different in any way from what is said in this newsletter.

Mr. Chairman, I am going to read a sentence from each of the letters so that you will be able to see the opinion of these banks. This would be a way of saving time because in this way I can show you what every President thought of it. I must say that there is only one bank, the Toronto-Dominion Bank from which I received no answer.

*(English)*

Mr. PATON: If I might come to the defence of my bank, I am quite sure that if your letter was received indeed by us, and that we have to establish, it would have been answered.

*(Translation)*

Mr. GRÉGOIRE: The other chartered banks, as well as the Bank of Canada and the Minister of Finance, all answered.

*(English)*

Mr. PATON: May I have a copy of your letter after the meeting is over and I will look into it?

Mr. GRÉGOIRE: I forget to whom I wrote it, I think it was to Mr. Lambert.



(Translation)

I got a reply in French.

(English)

The CHAIRMAN: We should establish that we are not talking about our own Mr. Lambert.

An hon. MEMBER: He is not that banker.

(Translation)

Mr. GRÉGOIRE: Mr. Chairman, this is the answer that I received from the Chairman of the Bank of Nova Scotia. We think however that the newsletter of the Royal Bank gives a precise description of the basic mechanism used for the creation of money. That is Mr. Nix's where he uses the expression the "creation of money". The Canadian Imperial Bank through its economic adviser, Mr. Crowe answers, on behalf of the chairman, by dealing with the description of banking operations by the Bank of Canada. It refers to the effects of those operations on the entire banking system. This is exact and quite rightly so. It states that the control of the purse strings belongs to the Bank of Canada. Nobody has expressed disagreement so far. The National Canadian Bank through Mr. Louis Hébert, shares the views expressed by the author of this document. There in another bank here which endorses this document. The fact that it sets out with tables in support are exact. The Bank of Montreal, through its Vice-President and General Manager, answers also. I would be quite ready to table the letter. Mr. Chairman, so that in view of the limited scope of this pamphlet it is quite a clear explanation of the essential elements of the mechanism for this play of money as officially defined, all of it controlled by the Bank of Canada.

The Royal Bank of Canada through its President, Mr. McLaughlin writes, "It is well understood that I am entirely in agreement with the text".

The CHAIRMAN: Obviously.

Mr. GRÉGOIRE: I did not get any expression of opinion from the National Canadian Bank. As far as the Banque Provinciale is concerned it says here: "Seeing that you are a customer in one of our branches we would be very happy to see you and discuss this matter with you". In fact I did not get any opinion from them. They said that since I was a customer—I financed my own boat through that bank. They own my boat, in fact.

The CHAIRMAN: You are a partner, so to speak.

Mr. GRÉGOIRE: It may be an indirect criticism. Perhaps I should invite the proprietors of my boat on my own boat.

Now, I would refer to the Minister of Finance. Mr. Sharp. He wrote to me and I quote: "In my opinion, this could surely achieve its goal as set out in its foreword. It is a simple and clear description of the manner in which the Bank of Canada operates, of the deposit liabilities of the chartered banks and of the money supply in Canada." There is no criticism, those views are endorsed.

Mr. Raminsky replied by sending me the document which was tabled at the Porter Commission.

So those are the preliminary remarks which I wanted to make, and here I would like to bring forth my original question again. I would like some information about the answer given by this brochure.

The CHAIRMAN: Just a moment. I believe it might be better, to give every member here an opportunity of making himself aware of the contents of all these letters. You can leave them with the Clerk, Mr. Grégoire, but it might help us to have these documents before us.

(English)

Mr. LAFLAMME: Mr. Chairman, I would like, at this point, to raise a point of order. I just would like to know if there is any one here who could on a blackboard, explain the process of the circulation of money from one bank to another so we can get through with those questions.

(Translation)

Mr. GRÉGOIRE: Mr. Chairman, I do have a table in this brochure. I think it is an excellent exposition of the system in four pages. I would like to sum up the table in a few minutes and then ask questions. This is how the Bank of Canada increases the bank deposits of the chartered banks and consequently the money supply. The chartered banks have reserves in the amount of 80 million dollars plus loans in the amount of 920 million: i.e. a reserve of 8 per cent. The next operation is this—

The CHAIRMAN: To clear it up a little bit, may I offer you a little suggestion. In summing up this text on page 4, it is quite possible that the Committee might think that you are using up the time available for the questions. If everybody in the Committee has this document, things might be a little different.

Mr. GRÉGOIRE: Just one moment, sir. My first operation deals with the initial supply, 80 million in money supply, 920 million dollars in loans. Second operation—the Bank of Canada puts 8 million dollars into circulation by buying securities. What happened at that time was this—these cheques, or these securities that is, bought by the Bank of Canada, were issued to the public. The public deposits then in the chartered banks. At that point the chartered banks had 88 million dollars in cash reserves plus 920 million out in loans, that is one billion 8 million dollars. The percentage of reserves has gone up to 8.73 per cent, which indicates that it is .73 more than before. With 8.8 million dollars in cash, deposits have to increase. This is what is written here in the brochure, because this must increase by 92 million dollars, up to one billion and some odd, to reduce that sum to 8 per cent. This is where the operation begins. What are the banks going to do?

—within the chartered banks and at that time the chartered banks had 88 million dollars in cash reserves, plus 920 million out in loans, that is a total of one billion 8 million dollars. The percentage of reserves have gone up to 8.73 per cent, which indicates that it is .73 more than before.

With 88 million dollars in cash, deposits have to increase, and that is what is written here in the brochure, because this must increase by 92 million dollars up to one billion and some odd to reduce that sum to 8 per cent. This is where the

operation beings. What are the banks going to do? We move then into a third stage. Banks acquire loans and extra securities in the amount of 92 million dollars, which increases their deposits by 92 million dollars. They do not have this 92 million dollars yet they will lend out 92 million dollars. These 92 million dollars accumulate in deposits within the system, and the reserve is thereby increased 100 per cent. This is said on page 6 on top of the page. Cash reserves are unproductive assets so that banks quickly use up their excess in supply to make loans or buy securities, which re-establishes the original level of depositors.

But I ask you then, as Mr. MacIntosh can tell you, is it not a fact that the 92 extra million dollars which has been loaned out, due to the simple fact that the Bank of Canada has put 8 million dollars into circulation, constitutes purely and simply—and the President of the Bank of Nova Scotia says as much—a creation of money or a creation of credit. The total money supply has been increased, in order to maintain the reserves at 8 per cent. That is the creation of 92 million dollars based simply on the fact that the Bank of Canada has bought in securities 8 million dollars. Is that not a fact, Mr. MacIntosh? Does that not explain the difference between the 2 billion 500 million dollars in circulation here, and the 80 million dollars out on loans made by chartered banks. Is that not simply a creation of money as the President of the Bank of Nova Scotia states here?

*(English)*

The CHAIRMAN: Mr. MacIntosh, would you care to proceed?

Mr. MACINTOSH: Mr. Chairman, it is an undeniable fact that credit expansion must take place as the economy grows. The fact that the assets and the liabilities of the banks are larger now than they were a year ago is a reflection of the fact that there has been an expansion. If you were asking us whether or not an expansion has taken place the answer is: "Yes, of course, an expansion has taken place." In fact if you will look at the table circulated by the governor of the central banks you will see the expansion of the near banks' assets has been even more rapid. I will refer you to the table which he presented, I believe, last Thursday evening where you will see that the assets of the trust companies have increased from 1960 to 1965 by a substantially larger percentage than the rate of growth of the chartered banks' assets, and the same applies to the mortgage loan companies, the caisses populaires and other institutions. If your question is: "Has there been an expansion?" The answer is "Yes."

The expansion process is initiated by the central bank because it wishes to see that the volume of credit in the country is appropriate to the needs of the economy and the process is set in motion by the central bank expanding its assets. That is perfectly true. It expands its assets whereupon the liabilities of the Bank of Canada to the chartered banks become larger and through this procedure, in a long process of making loans and acquiring deposits, the system expands. But, there is nothing peculiarly unique about the system that applies only to the banks.

Mr. GRÉGOIRE: Mr. Chairman, I do not think this is what I asked. I believe that there was an expansion of credit—you can see that by the statistics. Now, the Bank of Canada originated the expansion of credit with \$8 million. My



question is: Is it not a fact that after this expansion of \$8 million by the central bank the chartered banks continued that expansion by lending \$92 million which will create a term of credit and they will continue this expansion up to the limit of \$100 million. Now, even if the \$8 million of the expansion is due to the Bank of Canada the other \$92 million of expansion is due to the chartered banks by the creation of credit. That is the part I would like to have an answer on.

Mr. MACINTOSH: This would not necessarily take place if the near banks drew out some of the cash. It does not follow that the banks—

Mr. GRÉGOIRE: But, as I said, if \$8 million goes to the chartered banks as new reserves, would the chartered banks have the facility to continue that expansion 12½ times up to \$92 million—the money and credit they create?

Mr. MACINTOSH: They have the possibility of expanding so long as they are able to attract deposits.

Mr. GRÉGOIRE: Would they first consent to the loans or first attract deposits?

Mr. MACINTOSH: You cannot dissociate loans from deposits because the assets and the liabilities sides of the balance sheet are one and the same. They must balance; they are equal at the same time.

Mr. GRÉGOIRE: How, then,—

The CHAIRMAN: Mr. Grégoire, if you do not mind—

Mr. GRÉGOIRE: I have just one more question to complete. Now, then, how can you explain this. Here they say—and it has been confirmed by six managers or general managers or presidents of banks—and I will read it again in French because I have the French copy here.

The CHAIRMAN: Mr. Grégoire, just one minute please. With all due respect I do not know that you are being fair to the others taking part in the work of this Committee to reread something you have already read and which we have followed very closely. In fact, it would seem to me that while you and Mr. MacIntosh may end your case by agreeing to disagree, the members of the Committee I think have—

Mr. GRÉGOIRE: No, Mr. Chairman; please let me continue. Once you have said that loans and deposits are to be considered together—and here is what they say: "The banks will therefore use up any excess cash immediately by making loans or buying securities, thereby restoring the original level of deposits." So the loans will come first. When they have \$8 million they will then make loans and naturally as a consequence there will be in the whole system of the eight chartered banks according deposits but the loans will come first. Without any deposits they will create the loans and then the deposits will come as soon as there is a loan. Is that correct?

Mr. MACINTOSH: This would not happen if the loans are taken out in cash.

The CHAIRMAN: Perhaps I can assist you. This may seem strange to the Committee. Perhaps we can bring it down to this point: Are you and Mr. Grégoire not—I was going to say, saying the same thing, but this may be too much of a shock to you as a banker. If the loans are not taken out in cash and are entered on the books and are drawn on as cheques and so on and so forth, are

you not really on a point now where you are not really disagreeing as much as you, perhaps, think you are.

Mr. MACINTOSH: Well, no, I think, sir, we understand very well the nature of our disagreement, and I think, since I have the support of the Governor of the Bank of Canada, I am not willing to concede that there is no difference.

The CHAIRMAN: I think, in all fairness to the others taking part in the work of the Committee, we should conclude this area.

Mr. GRÉGOIRE: We are finishing in 10 minutes, so why not complete it?

Mr. FULTON: What does Mr. MacIntosh say. Mr. Grégoire has said: "Is this not so: that is what we have."

The CHAIRMAN: Can we have the unanimous consent of the Committee to permit Mr. Grégoire to continue until six o'clock?

Mr. FULTON: May I ask this: What is it that Mr. MacIntosh says happened. We have had Mr. Grégoire's version. He has asked you if you do not agree with it. You say: "No." But, I have not yet been able to satisfy myself as to how you briefly would describe what happened. What do you say happened when that \$8 million first came out.

Mr. MACINTOSH: These are high powered dollars that the government—

Mr. GRÉGOIRE: I would just like to ask him that question. That is what the Governor of the Bank of Canada described as high powered money—this \$8 million. When the Bank of Canada puts it into circulation, if it goes to the chartered banks, it will increase their reserves. If they do not make additional loans, will they increase their deposits up to the 8 per cent of cash reserves, or will they increase their deposits as they increase their loans by \$92 million. Is that a fact?

Mr. MACINTOSH: You have to distinguish between what would happen to the banking system as a whole and what happens to an individual bank in the system.

Mr. GRÉGOIRE: Let us take the banking system as a whole.

Mr. MACINTOSH: If we take the banking system as a whole, and suppose there is one bank in the whole system, then it is the same thing.

The CHAIRMAN: The concept in this—

Mr. GRÉGOIRE: Describe the system as a whole.

Mr. MACINTOSH: The Bank of Canada initiates this process by buying \$8 million in securities. Its assets are larger by \$8 million, its liabilities are larger by \$8 million, because the \$8 millions has been acquired by a bank, which had a customer who sold the securities to the central bank; the customer deposits the cheque on the Bank of Canada in the chartered bank; the chartered bank returns the cheque to the Bank of Canada; the assets of the Bank of Canada have increased \$8 million on one side, and its liabilities in the form of deposits of the chartered banks have increased \$8 million on the other side. Right?

If the bank makes a loan, it could make that loan in cash and the customer could take cash out, the \$8 million could be withdrawn by the borrower if there

are such borrowers who can borrow \$8 million, and spent by him or paid over to someone else. That person receiving the money would deposit it back in the same bank, or in the system, if you like; therefore while a loan has been made, the money has been returned to the bank and the bank now has a loan, the system's cash is unchanged; it now has a loan and it has a deposit. The process can continue being repeated until such time as the system as a whole is in a position where it has 8 per cent cash to its deposit liabilities. This is the nature of the process, but it is not a boot-strap operation. When you talk about the system, the deposits exist in the system, because they have nowhere to leak out of it, although I include there the near banks. When you talk about the activities of an individual bank acquiring cash, then all the money which it lends can be lost to another bank or another near bank and therefore it simply cannot lend what it has not got; it can only lend what it has on deposit. This process is the way the system works.

Mr. GRÉGOIRE: But if the loan is deposited in another bank, the other bank will be able to do what the first bank was not able to do, because it lost it the first time. But the whole system of banks together will be able to lend \$92 million, as long as they have an \$8 million cash reserve.

Mr. MACINTOSH: Ultimately the system will expand if the Bank of Canada chooses to make it expand, undeniably; I think this is the point of the system.

Mr. GRÉGOIRE: But it will be the chartered banks that will expand by \$92 million. Is that right. According to what is said here, when the Bank of Canada expanded by \$8 million, if it goes to the chartered banks, they can then expand it by another \$92 million by making loans.

Mr. MACINTOSH: Providing they acquire the money back on deposits.

Mr. GRÉGOIRE: And the whole system will acquire the deposit back?

Mr. MACINTOSH: If you include the near banking system with the chartered banking system, yes.

Mr. GRÉGOIRE: But the first that will come will be the loans and then the deposits will follow? Right?

Mr. MACINTOSH: No.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): May I ask a supplementary question of Mr. MacIntosh. Let us assume, Mr. MacIntosh, that when the Bank of Canada produces the much talked about \$8 million, that all those who have received the money from the Bank of Canada deposit it and, if in the experience of bankers they knew that next Thursday all their depositors would come and demand the money at the same time, could the banks then give larger loans than the \$8 million?

Mr. MACINTOSH: No. Mr. Cameron, they could not. What you are saying is quite right—if the borrowers took the money out in cash and put it in the mattress, that would be the end of the process.

Mr. GRÉGOIRE: Let us say you have \$19 billion worth of deposits in all the chartered banks, and if all the depositors of all the banks withdrew all their money at the same time, you would not have enough money to pay all the depositors, would you?



Mr. MACINTOSH: Certainly; the banking system works on a proposition that in the ordinary course of events, day in and day out, if they have a certain level of cash reserves, this will be sufficient to satisfy the requirements of their customers, and here again the system is not strange to Canada, this is the way the system works the world over.

The CHAIRMAN: Order, please, gentlemen. I think this would be a good time to recess. We will resume again at 8 o'clock this evening.

#### EVENING SITTING

The CHAIRMAN: I will call the meeting to order. Mr. Clermont?

*(Translation)*

Mr. CLERMONT: Mr. Chairman, do you not feel it would be preferable for the references which the member for Lapointe read into the record this afternoon, to be annexed to our minutes? He quoted certain passages here and there from various letters and also, I believe from a newsletter published by the Royal Bank. It might be a monthly bulletin, I am not sure.

The CHAIRMAN: I would like you then to move that those letters quoted by Mr. Grégoire and the bulletin also quoted by him and published by the Royal Bank of Canada, be officially added to our minutes for today.

Mr. CLERMONT: I would so move, Mr. Chairman, of course, with Mr. Grégoire's consent.

Mr. GRÉGOIRE: I will do more than consent. In fact I have said as much this afternoon. I would nevertheless ask the clerk to leave them with me until tonight, because I would like to have them copied before that, unless I am told that I will receive them before tomorrow morning. I would like the clerk to tell me this. Would a photostatic copy be adequate for the Committee's purpose, so that I may retain the original?

The CHAIRMAN: I believe so.

Mr. CLERMONT: Now, as far as the copy of the letter is concerned, will he table that in its entirety?

Mr. GRÉGOIRE: I will table the letters I sent to the Bank presidents. It is the same letter, so one copy would be adequate.

The CHAIRMAN: You need not table the original.

Mr. GRÉGOIRE: As far as the Royal Bank of Canada newsletter is concerned, I believe that we should ask the general manager of the Royal Bank of Canada, if he has any copyright on that.

The CHAIRMAN: That bulletin was circulated, I think, just to about every member of the Committee.

Mr. GRÉGOIRE: I have absolutely no objection to it being annexed to the minutes of today's proceedings.

*(English)*

The CHAIRMAN: Is there a seconder?

Mr. LEBOE: I second the motion.

The CHAIRMAN: I presume that the Royal Bank have no objection, either, to having a very interesting and useful document made part of our record for today. We are agreed, then.

(Translation)

Mr. GRÉGOIRE: May I also say we have an answer from the chairman of The Toronto Dominion Bank which I cannot provide, not having received it.

The CHAIRMAN: I believe this answer must be in preparation at this time.

(English)

Mr. PATON: Mr. Chairman, I would say for the record that we have not yet been able to trace receipt of this letter, but I have obtained a copy of the letter purporting to have been sent to us by Mr. Grégoire. I sent it on to Toronto tonight. It will be, I hope, in the hands of my President tomorrow morning, and I expect to receive a report from him tomorrow as to its receipt or non-receipt. Whether or not I can have a reply back by Thursday morning is debatable, because obviously it is a letter which requires a great deal of thought.

The CHAIRMAN: I am sure your bank will do its best and anyway, as long as it is not someone's loan payment which is possibly mislaid, we do not have to worry too much.

I think we should also have a motion to incorporate in our record for today the exhibit tabled by Mr. Elderkin setting forth the interlocking directorates of banks.

Mr. MORE (*Regina City*): I so move.

Mr. LAMBERT: I second the motion.

Motion carried.

The CHAIRMAN: I recognize Mr. Cameron, followed by Mr. Wahn and Mr. Comtois.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Thank you, Mr. Chairman. First of all, I would like to ask Mr. Paton a question that I hope will clear up some of the difficulties we have been having.

Is it correct, Mr. Paton, to agree with Mr. Gregoire that the chartered banks do, in effect, create money, but that they do so, not on the basis of any privilege granted through legislation but by virtue of the habits of depositors and long experience of lending agencies going back many centuries. The crux of it being that through long experience it has been discovered that only a very small percentage of those who deposit come on the same day to demand their money, and that if the habits of depositors were to change drastically in the future, either to the extent of more of them coming to demand their money at one time or fewer of them, then the banks' lending capacities would change at the same time? Is that a correct statement with regard to the expansion of credit?

Mr. PATON: Mr. Cameron, I would suggest that perhaps you and I should change places, because I do not think I could have put it any better than you have. In my mind, that is essentially what we do.

The CHAIRMAN: Would you yield for a supplementary question?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes.

Mr. GRÉGOIRE: Then, due to the circumstances mentioned by Mr. Cameron, you admit that you do, in fact, create money?

Mr. PATON: I do not admit it in essence, Mr. Grégoire. I feel that perhaps the purpose of your question is to imply that by a stroke of the pen I, or any other banker, or any group of bankers, can create money. I do not admit that.

I admit that the Bank of Canada, in its continuing monetary management in Canada, undertaking hundreds of transactions simultaneously, concurrently or consecutively, has a certain viewpoint in mind as to where the money supply is going to go, and we as the banks are the effective instruments through which they implement this policy. If the Bank of Canada decided that the money supply should be higher next month than it was last month, we will participate in it as a banking group with the near-banks. But the implication that if the money supply increases suddenly I would go out and lend more money is not correct. Remember, too, that before one can lend money one must have a willing borrower. It is not just a question of going out and lending money. You must have somebody who wishes to borrow it from you.

The CHAIRMAN: Is there ever a lack of willing borrowers?

Mr. PATON: In essence I would concur with Mr. Cameron's question, but I would still reserve the right to say that I do not create money merely by the stroke of a pen.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Chairman, to come back to some of the more pedestrian activities of banks, I would like to ask you, Mr. Paton, if you would perhaps expand on some comments you made earlier today with regard to compensating balances, which I understand are arrangements that banks make with their borrowers to cover the cost of servicing certain loans. Is that correct?

Mr. PATON: Servicing loan accounts.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Servicing loan accounts. Could you give us any idea how you arrive at the compensating balance that should be called for in any particular circumstance?

Mr. PATON: Compensating balances, Mr. Cameron, can be considered as one phase of banks' methods of recovering costs of funds. Direct fees can be considered as another.

As we indicated this morning, we have compensating balances in other areas of our bank operations; in the operation of deposit accounts, in the providing of letter of credit facilities and in other ways. Recovery of our costs sometimes takes the form of compensating balances, but not at all times.

In other cases a fee is charged for issuing letters of credit or collecting drafts drawn for collection, and all the various facilities that we provide through the many conglomerate operations of a bank.

There has probably been a greater use of compensating balances in recent months compared to the past year or year and a half. It has become more noticeable, it has become more general in the way of attaching compensating



balances to the cost of operation of the loan account, which does incur administrative costs to the banks.

I would say there is no specific yardstick by which we suggest to our customers that this is a condition of supplying this line of credit. For example, we might ask them to pay a fee where we have made a commitment that at such and such a time, if, as and when needed, we will provide them with a line of credit. We sometimes get a recompense from that through a standby charge, a percentage charge, which firms up the commitment that we would make to the customer. It varies. It ends up, perhaps, with a reasonable similarity among the various charges by which we recover the additional costs of doing business which are constantly with us, and one of the additional costs, of course, is the cost of the money which we have loaned.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would it be fair to say, Mr. Paton, that the increase which you have mentioned recently in compensating balances has some correlation with the stiffer competition the banks have been getting from near-banks?

Mr. PATON: That would be a contributing factor, yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): In other words, this was a means by which, with the 6 per cent ceiling, you were able to recover what you considered to be a more equitable compensation for your operations. Would that be right?

Mr. PATON: To a less extent we do not associate it with the interest costs which we are charging the customer.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Possibly the customer does.

Mr. PATON: It is possible, yes. He is looking at the net cost. It is the same, perhaps, as on the personal loan charges, with the cost of money expressed in a per annum rate, but we do not in any way associate that with our interest charge. I think perhaps my colleague Mr. Coleman might like to enlarge on that, if I may make the suggestion, Mr. Chairman.

The CHAIRMAN: Yes. Would you go ahead, Mr. Coleman?

Mr. COLEMAN: Mr. Chairman and Mr. Cameron, Mr. Paton has covered this very well but I think there is one feature I would mention. These balances are for recovery of costs. On small accounts we have determined in our bank in order to give a customer one free cheque on a savings account on which we pay interest there has to be a \$100 balance for the quarter. In a current account on which we do not pay interest, we give one free cheque for every \$50 of monthly balance. When you get to a larger account, then you have to analyze it and take all factors into consideration. How much coin do you handle? How big are the deposits? How much time does it take to handle this customer's account? This is how you arrive at the cost of maintaining the account. Then this cost can be met by the customer either on a figure compensating balance basis—calculated at a figure of what money is worth—figure or on a service charge basis, or both. You say, "If you do not want to maintain a compensating balance you must pay a service charge of so much."

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Are there any figures available as to the volume of compensating balances and service charges which the banks make?

Mr. COLEMAN: I would say there are not, Mr. Cameron.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well then, could I ask you this. When the interest ceiling is removed can we expect that these other methods of recouping costs will be abandoned and they will be incorporated into the interest rate?

Mr. COLEMAN: I would say not, sir. This does not relate to interest rate. We are charging for the cost of the activity in the account.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I must say I find it rather difficult to understand why it does not relate to the interest rate because the interest rate is at least in part surely, set in relation to the cost?

Mr. COLEMAN: No.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No?

The CHAIRMAN: Mr. Cameron, could I interrupt here? May I refer you, sir, to page 3 of your submission. As a basis for supporting the removal of the 6 per cent ceiling, clause (b) on page 3, you adopt this quotation from page 364 of the Porter Report. I will read it: "More specifically, 'the ceiling stands in the way of flexible lending by the banks in that it frequently prevents them from making loans on which higher rates must be charged to cover administrative costs and risks.'"

Mr. COLEMAN: That is right, but I do not think that is relevant, Mr. Chairman.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It seems to be in conflict with what you told me just now.

Mr. COLEMAN: No. That is simply a case of an applicant coming to us for a loan who is not a 6 per cent risk, but may be a 7 per cent risk or perhaps an 8 per cent risk. If we cannot charge the proper rate we cannot take care of that borrower.

The CHAIRMAN: This is not what the quotation says. You have adopted this in your brief. In other words, you have incorporated these words as your own, which indicate that one reason why you want to charge a higher rate is to cover administrative costs and risks, which you mentioned. Now, what do you include in administrative costs?

Mr. COLEMAN: The general operation of the account.

The CHAIRMAN: Yes, but how is that different from what you have just been describing to Mr. Cameron as the cost of servicing the account?

Mr. COLEMAN: Mr. Chairman, all I can say is that when we lend money the rate is fixed. Today it is 6 per cent; that is the prime rate.

The CHAIRMAN: Yes.

Mr. COLEMAN: In the past for many years the prime rate was  $4\frac{1}{2}$  per cent and the rate charge varied with the degree of risk involved. It had no relation whatever to the activity in the customer's current account.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well, then, would you answer this question for me. I recall very clearly in the last revision of the Bank Act there was only one chartered bank which was in the personal loan business and that was the Bank of Commerce, as it was at that time, and they were charging 12 per cent; 6 per cent was officially interest and 6 per cent was officially service charges. The reason given for that 12 per cent rate was the cost of servicing the small loans which would be involved in the personal loans. This again seems to be at variance, and you do consider the interest rate in the light of the cost of servicing a particular loan.

Mr. COLEMAN: The bank to which you referred and the other banks in personal loans today charge 6 per cent interest, and they add service charges to compensate for the operation of that account.

The CHAIRMAN: Is the operation of the account not included in the administrative costs?

Mr. COLEMAN: Not in that type of small loan, no.

The CHAIRMAN: What about a bigger commercial loan?

Mr. COLEMAN: It is completely different. The average consumer loan applicant comes in to get a loan and there is very little activity in his account. Your big borrower, usually, is a corporation where there are large deposits; they might have par privileges; you might have to put up payrolls for them, or any of the different services we provide.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would you then answer this for me? If this is the case, you pay no attention in setting your interest rates to the cost of servicing a particular loan account and your interest rates are set on some other basis, then what is the explanation for the increase in the instance of compensating balances, to which Mr. Paton just referred, if it is not that you have to compete with other lending and deposit receiving institutions, which again brings it to the question of setting the interest rate.

Mr. COLEMAN: Why has the practice in compensating balances been increased? Is that your question?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes.

Mr. COLEMAN: I think it is purely and simply because the banks have finally realized that they are operating many, many accounts at a loss and they are now putting them on a proper basis.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): And yet Mr. Paton told me just now that he thought there was some connection between the increase in the demand for compensating balances and the rise of the other lending institutions. Your whole argument for the removal of the 6 per cent ceiling was that you had to compete with these other organizations.

Mr. COLEMAN: That is right.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Therefore the compensating balance apparently takes the place of an increase in the interest rate, which you are not now legally allowed to impose. Is that not right?



Mr. COLEMAN: Your debit interest rate is related directly to your credit interest rate. It is related directly to the cost of money, and the cost of money is so high today that we cannot compete with other institutions who are able to pay more than we can charge and can lend the money out at 8 or  $8\frac{1}{2}$  or 9 per cent, which we cannot do.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): So you have been obliged to increase your demand for compensating balances?

Mr. COLEMAN: Not for that reason.

Mr. PATON: I think, Mr. Chairman, if I may interject, we have to divide it up into two phases. Money has its true cost and services have their true cost, and we are now identifying these two separate costs more closely than we did in the past.

The CHAIRMAN: Why is it, sir, that in this quotation you have adopted you apparently combine both costs under the heading of higher interest rates?

Mr. PATON: Mr. Chairman, if we had written the commission's report we would probably have eliminated "to cover administrative cost" and said:—"must be charged to cover risks".

The CHAIRMAN: But you adopted this, sir, in your brief.

Mr. PATON: We are still prepared to stand by the brief for the simple reason that in quoting it would not be in order or ethical to quote the Porter Commission Report without completing the section. It would be unfair, I think, to have quoted this as coming from the Porter Commission without completing the section.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Was it necessary to quote it, Mr. Paton? Could the Bankers' Association not have stated it in terms more acceptable to themselves?

Mr. PATON: Mr. Cameron, I had a speaking engagement in Toronto yesterday, as you are aware, and I quoted the Porter Commission there because I indicated to the audience that they might conceivably consider a banker as being somewhat biased in his views if he expressed it in his own language.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then Mr. Paton, I can only assume that you have adopted the Porter Commission's view.

Mr. PATON: That is correct, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): So you must accept this position put out by the Porter Commission and that you do consider interest rates cover all these considerations.

Mr. MONTEITH: When did the practice of charging for administering accounts and the compensating balance, and so on, develop? Has it always been in the banking system or has it become more prevalent in latter years?

Mr. PATON: I think the answer Mr. Monteith, is yes in both instances. It has always been in the banking system, and certainly since my time we have had compensating balances for various services and it possibly has become more prevalent in recent times because we are identifying our costs and perhaps endeavouring—

The CHAIRMAN: You are becoming more cost conscious.

Mr. PATON: Yes, certainly.

Mr. MONTEITH: Maybe your experts have gotten around it. They had to find a way to make a little money.

Mr. PATON: No. I think what we have done is become conscious of the fact that we have been giving services in the past at less than cost and we have had to establish—with the pressure on us when money costs rise—other areas where we could meet this additional cost.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I would now like to turn, if I could, to the question of the inner reserves and the misgivings which the Bankers' Association has about their revelation. I am interested in the first place, Mr. Chairman, to note the somewhat different emphasis this time than was the case 12 years ago when we were told that the whole financial house would collapse about our ears if this was to be revealed. I am still unable to understand why the banks are still considering it a dangerous thing to reveal the size of their inner reserves, and Mr. Paton this afternoon suggested that while at the present time in a period of economic buoyancy there might not be any particular danger to the confidence the public held in the banks if losses were revealed, in periods of more depressed economic activity there might be a loss of confidence.

The question I would like to ask Mr. Paton is this: during the period, we will say, from 1934 to 1939, which was the first period in which the central bank was set up, were you aware of any loss of confidence on the part of the public in the banks?

Mr. PATON: This is going back quite a way, Mr. Cameron, and I do not know that I feel particularly qualified to answer that question. I know there was a very grave concern. I think there was a substantial need to use a good portion of the reserves which the banks at that time held.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The point of my question is this, Mr. Paton. Do you and your associates not think that perhaps a little more frankness with the public with regard to your operations would not decrease the public's confidence but that it might well increase it?

I further suggest this to you, Mr. Paton, that the very fact that you are reluctant to reveal certain figures creates in the public's mind an image of something going on about which they are not being told. I wonder if you have ever thought of this, that it would be to your advantage to put your cards firmly on the table and say, "Yes, we made a bad guess then, we lost some money there and we had to put up inner reserves to cover it". Do you really think that would destroy confidence in the banks?

Mr. PATON: My answer would be that there would be a very great risk that it would have just that effect, dependent on the time that such disclosures would be made public. I see little difference between the situation at this revision and the situations in 1954 and 1944, at which time it seemed to be generally conceded that it was a reasonable position for the banks to take that they have permissible reserves for appropriations, in anticipation of possible losses in loans and investments, under complete control of the Minister of Finance through the Inspector

General with a top limit on such reserves so that the banks themselves could not freely put inside any amount of reserves which they so wished. The shareholders' auditors of the banks and the Inspector General were charged with the responsibility to see that these reserves were adequate but also to see that they were not excessive.

I think in the annual statements of the banks, with the reported profits which are shown after these provisions have been made, there has been a reasonably satisfactory disclosure of the banks'—and I speak of the banks as a group—progress over the years.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I could see, Mr. Paton, where the rest of the business community might regard you with a certain amount of envy in that your loss rate over 25 years was .151 per cent, but I do not suppose anyone would consider you were probably a shaky institution because you had had this level of losses.

Mr. PATON: I wonder, Mr. Cameron, if I could suggest an analogy in a manufacturing concern which, during the year, decides to go into a new product and the product fails dismally. They acquire or manufacture, say, \$200,000 worth of this particular line, and it is a complete failure. At the end of the year this is charged to their costs of production. The particular loss of that amount is not disclosed to anybody anywhere other than the principals of the operation.

The suggestion here is that the banks would disclose the loss on every transaction in which they became involved from November through to October, their fiscal year. There are many other concerns, corporations that have a substantial write-off for various reasons, receivable, losses, decline in inventory values and so on, which are shown as a net figure, and you have no idea when you look at their statement as to what actually went on during the year. In the banking business public confidence is particularly important. Furthermore we feel that it would not be equitable to suggest that the banks disclose every dollar they lose through investments or lending.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well, let me put this question to you, Mr. Paton. Did you at any time during the last 25 years consider that the rate of loss had actually impaired the stability of the banks?

Mr. PATON: I would say, no, sir. Mind you, I have no specific knowledge of the other banks. I think I could answer quite unequivocally and frankly, that there has been no such situation at all at any time.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Do you not think the general public would take the same view? With regard to the fairness of asking banks to reveal their losses and not to ask other people to do so, I think you forget, perhaps, that while it is perfectly true, as I pointed out in my first question to you that some of the illusions about what banks are doing are illusions, nevertheless, you do occupy a key situation in our economy. You do have certain privileges—not the ones that Mr. Grégoire imagines they are—but they are, I think, confined to one thing, the right to use three words: banks, banking and banker. They are an extremely valuable privilege that is granted by the parliament of Canada. Do you not think the Canadian people have the right to know how this key sector of our economy is operating? Do they not have a right to know what amounts you are being allowed to set aside to cover losses on



which, incidentally, you pay no tax and therefore the taxpayers of Canada are subsidizing you to that extent. Do you not think it is right the people of Canada should be told this?

Mr. PATON: I think perhaps it would be wrong of me to leave that on the record without an endeavour to rebut it. We do not escape tax. These inner reserves cannot be brought out without paying the tax.

Mr. CAMERON: Oh, I know, they cannot be brought out without being taxed.

Mr. PATON: These reserves are pre-tax reserves but at the same time, as they are brought into the rest account or the surplus account of the bank, then automatically tax at a probably higher rate than it was when the reserves went in would be exigible.

Mr. LAFLAMME: May I ask a supplementary question? You are not paying taxes on your hidden reserves?

Mr. PATON: No, sir. They are a pre-tax transfer to our inner reserves; that is right. But, before they can be disbursed eventually, either being brought out into the rest account or disbursed in the form of dividends, full tax is paid. Of course, when they get into the hands of the shareholders, then they have to pay tax, too.

Mr. WAHN: May I ask a supplementary question that relates specifically to the question that has been raised? Is it fair to say that the amount of the inner reserves are probably increasing year by year so that in fact you will not pay on your inner reserves if this continues?

Mr. PATON: The eligible assets on which these reserves are permissible are growing substantially year by year. I think a percentage table of our reserves over the last number of years would show that they are on a substantially decreasing amount in relation to the risk assets to which they are applicable.

Mr. WAHN: I am not sure I understand the answer. Are you saying that you have, in fact, taken money out of inner reserves and paid tax on it, in excess of the amounts you have put into inner reserves?

Mr. PATON: From time to time, banks transfer from inner reserves to the rest account. When that transfer is made and it is shown on the statements of the bank, tax is paid on the amount that is brought out.

Mr. WAHN: But has the net amount of your inner reserve been increasing in recent years?

Mr. PATON: The net amount, dollar-wise, has been increasing, yes.

Mr. WAHN: Then there is a net tax saving, in other words?

Mr. PATON: Percentage-wise it has been decreasing.

Mr. WAHN: But the amount has been increasing?

Mr. PATON: The amount has been increasing.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): And there has been a continuing amount there on which you have not paid taxes?

Mr. PATON: That is correct.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I think that does validate my suggestion that the taxpayers subsidize you to that extent?

Mr. McLEAN (*Charlotte*): Does not the Minister of Finance oblige you to take certain amounts out of your reserve and pay tax on it?

Mr. PATON: No.

Mr. McLEAN (*Charlotte*): I notice in the bank statements you are paying more taxes than I can see in the bank statements. Are the banks taking out their reserves and paying taxes on it?

Mr. PATON: No, not necessarily.

Mr. McLEAN (*Charlotte*): Your statements do not agree then. You are paying more taxes than you should be paying.

The CHAIRMAN: Mr. McLean, we have been accepting short supplementaries but—

Mr. McLEAN (*Charlotte*): I just want to say that they are taking amounts out of the reserve and they are paying higher taxes than if they paid the tax when the money went into the reserve. It is circumstances which force them—

The CHAIRMAN: May I ask the Committee to return to the orderly procedure they have been following up to now? I think the time allotted to Mr. Cameron, even taking into account the various interruptions, has gone by and I would like to—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I will take up some more time later.

The CHAIRMAN: I am sure you will have ample opportunity.

Mr. MORE (*Regina City*): I have one supplementary before we leave this question, Mr. Chairman.

The CHAIRMAN: If it relates to the questions asked by Mr. Cameron.

Mr. MORE (*Regina City*): It relates to the question asked by Mr. Cameron with regard to your losses. If you lost \$12,500 on any account, would you take \$12,500 out of your inner reserve or would you take \$1,000 out of your inner reserve?

Mr. PATON: If we lost a loan of \$12,500 we would have lost \$12,500 hard cash. It might come from our current earnings during the year or from our reserve appropriation. I prefer to call it appropriation account rather than reserve account. But it would be \$12,500, it would not be \$1,000.

Mr. MORE (*Regina City*): I realize that but how much do you take out of this inner reserve to cover this \$12,500 you lose?

Mr. PATON: The full amount of the loss is a charge to the bank's operations.

The CHAIRMAN: Mr. Wahn?

Mr. MONTEITH: Mr. Wahn agreed that I might ask one supplementary here on the same topic, Mr. Chairman. I am assuming that the \$12,500 that was mentioned would be written off at the time but that at each year end you reassess your requirement, is that correct? When you prepare your financial statement at the end of each year you have assessed your position as far as the reserves requirement is concerned? When does the Inspector General look at this, after your statement has been made public and so on? I am assuming he would not have time before.

Mr. PATON: No, he makes his inspection at his convenience. I would like to point out that the transactions we undertake at the fiscal year end are limited by the "par of reserves" which the Inspector General referred to in his evidence and of which he produced a table for the Committee showing what is covered by that expression. If the par of reserves of a bank was at X dollars and they already had X dollars in their position, then they would not be able to transfer inside an amount additional to that.

Mr. GRÉGOIRE: May I ask a supplementary?

The CHAIRMAN: Only if Mr. Wahn will yield because it is his opportunity to question.

Mr. WAHN: I will be happy to yield, Mr. Chairman.

The CHAIRMAN: You are the soul of gentility this evening, Mr. Wahn.

Mr. GRÉGOIRE: It is a short supplementary question. Even if you have lost \$12,500 you would be able to lend it again to equalize deposits—

The CHAIRMAN: Order, please. I do not think we should have a process of creeping supplementals. It is really turning away from the orderly consideration of the matter. Now, Mr. Wahn?

Mr. WAHN: Mr. Chairman, I have several questions which are related to the desirability of increasing competition which was stressed so much in the Porter report and in a number of submissions which have been made to members of the Committee. Mr. Paton, am I right in thinking you are in favour of legislation which will encourage greater competition with regard to services provided by banks and near banks?

Mr. PATON: Yes sir.

Mr. WAHN: My understanding is that in the past, at any rate, some of the chartered banks have had substantial share interests in trust companies and they have also participated financially with other companies in companies that deal in mortgages: would that be correct? As an example, I have been told that a substantial interest in Canada Permanent Trust is owned by Toronto-Dominion and that a substantial interest in Eastern Chartered Trust is owned by the Bank of Nova Scotia and there is a close affiliation of some sort between the Bank of Montreal and Royal Trust and between the Royal Bank and Montreal Trust and between the Canadian Imperial Bank of Commerce and National Trust, and perhaps other trust companies. If in the past the chartered banks have been able to in effect, participate in the trust and mortgage fields through subsidiary companies or through share investments in other companies, why has that method been unsatisfactory? Is there some inherent advantage that a bank has that makes it desirable that it should be able to participate as a bank in the trust business, or in the mortgage business, over and above the advantage it would have if it participated through a trust company subsidiary or a mortgage company subsidiary? Do I make my question clear?

Mr. PATON: The import of your question, Mr. Wahn, is, would the banks prefer to be directly in the trust business and mortgage business as a bank and have a division or department operating as such or would their preference be to have an association with trust companies through share ownership or perhaps



through other connections. Of course, it is difficult to speak for the other banks and it is also difficult to assume just what the relationship is between these other banks and the trust affiliates with which their names have been associated. As you mentioned, someone has said that there are indications that there is a share ownership or other connection. I think these transactions were undertaken at a time when the direct facilities were not applicable and open to banks and it seemed a measure of good business judgment to participate in these operations in the manner in which we have done.

I think there are two separate groups—those banks that have equity interests in trust companies, of which my own bank is one, and those where there is simply a long-standing relationship between trust companies and banks. I think you mentioned the Royal and the Montreal Trust and the Bank of Montreal and the Royal Trust. These have been associations, the nature of which, I myself am not fully familiar, but they have associations that linked their interests in one shape or form over the years.

I would say that if the Bill No. C-222 provides the additional facilities indicated here which would let us get into the mortgage business—although there is no reference at all to participating directly in the fiduciary angle of a trust company—and if legislation was to be brought in that particular area it should at least recognize existing situations which were entered into in good spirit and proper manner and have been good for the economy. I do not think there is any doubt that competition between trust companies—trust versus trust—has possibly stepped up as a result of the participation of the banks in the companies you mentioned.

Mr. WAHN: Following from that, Mr. Paton, in your knowledge of the banking business, if the banks are given authority to go into the trust and mortgage fields, will the bank have a competitive advantage in the trust field over a trust company or in the mortgage field over a mortgage company simply because it is a bank. In other words, are there any special privileges which banks have which would give them an advantage over the trust companies and mortgage companies in these respective fields?

Mr. PATON: No; I would say that if the trust powers or facilities were accorded directly to the banks, then one would automatically expect banking powers and lending powers should be permitted to the trust companies. Our basic approach all through appearances before the Porter Commission was that we were not wishing at all to put any limitations on other institutions competing with us but that the rules be the same for all of us. Naturally, if new provisions were allowed to banks we would anticipate there would be a *quid pro quo* for the trust companies or the other near banks.

Mr. WAHN: Perhaps it is in the brief but I did not see it. Are you in favour of deposit insurance for banks and near banks as provided in the proposed legislation?

Mr. PATON: We did not include this subject in our brief. However, we have a summary here which sets out fairly concisely and coherently our viewpoint with regard to deposit insurance. I think we have enough copies and we would be very glad to have that distributed, Mr. Chairman, if this would be acceptable?

The CHAIRMAN: How long is that, Mr. Paton?

Mr. PATON: It is four pages.

The CHAIRMAN: Mr. Wahn, what is your wish? Would you like this circulated and we can ask questions later or would you like to have it given as an answer to your question?

Mr. WAHN: I think the former would be quite satisfactory, Mr. Chairman.

The CHAIRMAN: Then I would ask you, sir, to have it circulated to members of the Committee as soon as possible.

Mr. PATON: I think we have it available here, Mr. Chairman, in the required number of copies.

Mr. WAHN: Also, Mr. Paton, representations have been made to some of us, at any rate, that trust companies and near banks should be admitted to the bank clearing house privileges. Do you have any views on that?

Mr. PATON: I think the question regarding clearing house was raised this morning and I indicated there was a very decided misconception with regard to the clearing system and I might be able to—

Mr. CLERMONT: I asked that question but I do not think I got a reply, because you stopped the question at that point.

The CHAIRMAN: That is true. I think we had reached the stage where you had had a reasonable share of the time that is allotted. It depends on what you and Mr. Wahn would prefer. I do not think we have ever adopted a procedure where a question asked by one person could not be asked by someone else.

Mr. CLERMONT: It is not that, Mr. Chairman, it is only to correct Mr. Paton, because I do not think he gave a reply this morning.

Mr. PATON: I was going to say, Mr. Clermont, that you touched on this subject just at the expiration of your time and the Chairman suggested that we could come back to it. I think I indicated that I am anxious to have a description of the clearing system because the direct answer to your question, Mr. Wahn, is that these people are members of the clearing system through the chartered banks. I am referring to the trust companies and the near-banks. Would you like me to spend a couple of minutes on this?

An hon. MEMBER: Mr. Paton, I would like to ask if credit unions are one of the groups who are enjoying these facilities, too?

Mr. PATON: Yes, Caisse Populaire, credit unions, Province of Alberta treasury branches, Ontario savings office and trust companies. All use the clearing system. I will be as brief as I can. I think it might be helpful, in giving a description of the clearing system, to say that it is composed of two parts; the first is the clearing system, which consists of all Bank of Canada agencies and all chartered bank branches, sub-branches and sub-agencies in Canada. There are two functions of the clearing system, one of which is the process of a physical transferring of documents between each branch bank in Canada. This function is performed by about 5,700 bank branches, sub-agencies and sub-branches in Canada and almost the entire cost of the clearing system—and it is substantial—is incurred in performing this function. The exchange of documents among

bank branches through this myriad of towns and hamlets in Canada is between the branches of the banks represented in each particular area. That is the clearing system's first function.

The second function is the process for the settling of the balances on transactions between banks. Now, taking part in this process are Bank of Canada agencies and chartered bank branches at 9 clearing house points, chartered bank branches at 42 other clearing house points and 1,359 non-clearing house points. The work and cost involved in this area of the clearing system is negligible. This is simply the settling of the balances on transactions between banks. The role of the Bank of Canada in this process is to assist in the formal settlement of balances through the 9 points where the Bank of Canada has offices. We extend clearing privileges to the near-banks, and I know of no instance where we have balked at this and refused to do so. The payment orders drawn on near-banks by their customers are processed through the banks' clearing facilities. We also handle, for the near-banks the clearing of items drawn upon the chartered banks, which are negotiated by the near-banks for their customers. The number of payment orders handled by the banks' clearing system was 33.7 million. This is the number of items during 1963. Naturally they will have increased by this time.

We make these clearing privileges available to the near-banks on what I think are indisputably reasonable terms. They are subject to approval simply by whichever bank has the account of the specific near-bank—which recommends them for admission to membership, and the recommendation from their bank is invariably accepted. If the general manager of the bank holding the account recommends it, there is no question of them being blackballed or in any way refused. The arrangements a near-bank must make to obtain access to a clearing house includes the opening of accounts with one or more chartered banks to which these payments are debited. It is essential that they do have a bank account to which these orders can be charged.

The near-banks pay for their access at no more than cost. This consists of fees for local clearing items and for orders debited to the account, and some near-banks pay annual fees at points where the clearing house is established. We feel the royal commission recommendations on this particular point were not too well outlined. Perhaps there was a misunderstanding of the function of the clearing system. The royal commission recommendations on pages 393, 394 and 170 state that all banking institutions should be required to hold their reserves at the central bank. All banking institutions will be able to settle their clearings at the Bank of Canada, rather than being required to make arrangements with one of the present banks. The Bank of Canada would thus have to equip itself to act as a clearing agent for institutions in the centres where they are not represented.

The clauses of the Canadian Bankers Association Act, which is a federal act under which the association operates, give the association the right of operating clearing houses. This should be repealed, according to the Porter recommendation, and an association of all clearing institutions formed to manage the system. But the main point we must remember here is that the total cost of this clearing system has nothing whatsoever to do with the settling of the balances. It is the cost of the physical sorting, listing and transferring of the physical items for each specific point within the banking system which predominates. A note has been



handed to me stating that the annual cost of this transit process within banks is \$33 million and the annual cost of the clearing houses is \$60,000, so it can be seen that the clearing house cost is relatively moderate.

There seems to us to be several reasons why the royal commission recommendations are not well founded. This may be a bit too strong but they seem to be based upon a commonly held misconception of the operation of the clearing system. The C.B.A. has no right to operate a clearing system, as was mistakenly assumed by the Commission. It is empowered to establish clearing houses in Canada, but the banks may or may not choose to become members. It is not incumbent upon a bank to join a clearing house. The Association does not have the power nor does it in fact operate the clearing system. It is the banks themselves that operate it by virtue of the banking system.

The near-banks obtain the clearing services at no more than cost and it is difficult to see how bringing the Bank of Canada into this operation would provide more favourable terms. The entry of the Bank of Canada into the clearing system would affect only an insignificant part of a whole number of items to be cleared daily by the bank. The daily items handled by the near-banks would be about 60,000 as compared to 3 million by the banks.

As I have said before, the real cost of clearing is incurred within the branch system of the banks. The expense of inter-bank clearing and settlement is negligible. I hope that clarifies the situation.

Mr. WAHN: I have one final question, Mr. Chairman. It is my understanding that Canada's legislation is more restrictive than other major banking countries, specifically the U.S.A. and England, in permitting foreign banks to operate in the country by way of agencies, branches or subsidiaries. I also understand the Canadian Bankers Association, as an association, has not reached any decision publicly, at any rate, as to whether or not it would be desirable to have more competition within Canada from foreign banks. Is it fair to say that perhaps some members of the association are in favour of more competition from foreign banks and other members of the association are opposed to more competition from foreign banks, and that is the reason the Canadian Bankers Association have not come out one way or the other on this particular point?

Mr. PATON: Mr. Wahn, I would say—and this has been a subject which has been thoroughly discussed among Association members—that there is not a degree of unanimity on this subject. This was the reason that we did not include it in our brief. There was no reference made to it in Bill No. C-222, as we have it in front of us, and we confined our references in the brief itself to the clauses in this act. This is a very complex subject. It is one that needs very thorough study. Once legislation is introduced into the Bank Act it will be very difficult to amend and change. Before a composite view could be arrived at it would need very, very close study. I would like to suggest—and I think I speak on behalf of the Association—that with the different gradation of views on this whole subject more than one bank would, in all probability, be anxious to present their views on this particular subject. At the appropriate time, subject to the Committee's approval, I think you would find quite a few of the banks would be anxious to have an opportunity to give their views in that connection.

The CHAIRMAN: Before recognizing Mr. Comtois and then Mr. More, I just want to ask Mr. Paton a few questions about the clearing system. First of all, who actually manages this?

Mr. PATON: Let us assume we have a six-bank town, and let us take Windsor as an example. I think we can assume there are 35 or 40 branches. There would then be a central clearing location and it may well be the office of a particular bank. The location may well rotate every year.

The CHAIRMAN: Do the near-banks have any say in the administration of the clearing system?

Mr. PATON: No, sir.

The CHAIRMAN: What are the fees which must be paid for the use of the clearing system?

Mr. PATON: Do we have any statistics on that?

Mr. PERRY: There is quite an extensive list.

The CHAIRMAN: Is this a tariff that is available for inspection by the public?

Mr. PATON: No, and I do not know that it ever has been.

The CHAIRMAN: Why not?

Mr. PATON: I do not think there has ever been any request. The interest is strictly between the near-banks and the banks, and I think you would find—

The CHAIRMAN: Can the near banks see this tariff?

Mr. PATON: They know what they pay themselves.

The CHAIRMAN: Do they know what they pay?

Mr. PATON: There is no specific assessment. The major cost in this operation is the exchange of cheques on banks. The cost of this is absorbed in the day to day operations of the respective banks. Mr. Perry, am I off the beam on that?

Mr. PERRY: In our brief to the Royal Commission we have listed most of the charges. The main one is 5 cents per order.

The CHAIRMAN: Here are the charges for trust and loan companies.

Mr. PERRY: Yes—as you see they are in our brief to the Royal Commission.

The CHAIRMAN: I will look at it later.

Mr. PATON: It starts on page 116.

Mr. CAQUETTE: Mr. Chairman, can we have an answer as to whether the chartered banks are paying the near-banks any charges for the clearing of the chartered banks' cheques that are cashed or presented to the near-banks?

Mr. PATON: Mr. Lavoie, could you answer that question?

An hon. MEMBER: It is the other way around.

Mr. CAQUETTE: Are they paying anything to the near-banks for the clearing of your cheques?

The CHAIRMAN: In other words, if a Royal Bank cheque is presented—

Mr. PATON: The answer is no.

(Translation)

Mr. LAVOIE: To answer your question, Mr. Caouette, with regard to near-banks, you were probably referring to the Caisses Populaires in the province of Québec, you are thinking of those, are you not?

Mr. CAOINETTE: What did you say?

Mr. LAVOIE: You are dealing with the Caisses Populaires in the province of Québec?

Mr. CAOINETTE: Yes.

Mr. LAVOIE: Well, in that case I might say that they have their own clearing system within themselves—

Mr. CAOINETTE: Of their "Caisses"?

Mr. LAVOIE: Of their "Caisses".

Mr. CAOINETTE: But I am speaking here of the relationship between the bank and the "Caisse".

Mr. LAVOIE: The clearing of orders is done within the Caisses' own system, then it is sent along to the banks and it is the *Banque provinciale du Canada* which is the clearing agent for the Caisses populaires. The rate is five cents per item.

Mr. CAOINETTE: You ask the "Caisse" to pay that?

Mr. LAVOIE: Yes.

Mr. CAOINETTE: But when the "Caisse populaire" exchanges its cheque from the *Banque provinciale* or other banks, is it paid by the *Banque provinciale* at that time?

Mr. LAVOIE: No, the charge is made at the time the customer cashes his own cheque.

(English)

The CHAIRMAN: Just let me complete this question. Do you have a figure for the total cost of operation of the clearing house system?

Mr. PATON: Mr. Chairman, I will ask Mr. Perry to answer that.

Mr. PERRY: The figures I gave Mr. Paton a short time ago reflected the two elements of cost. One was the cost of operations within the banking system, which was \$33 million.

The CHAIRMAN: That figure is \$33 million, and the annual cost of the clearing houses is a figure of \$60,000.

Mr. PERRY: If you take the 51 clearing centres that averages about \$1,000 each, so you can see how little it is for each centre.

The CHAIRMAN: Do you have a figure for the total amount paid by the near-banks in fees?

Mr. PERRY: Part of what they pay would be included within the internal cost of the banking system.

The CHAIRMAN: Do you have the total figure? Perhaps I can pass on to Mr. Comtois and you can inform us later.



(Translation)

Mr. COMTOIS: Mr. Paton, it would appear that we may infer from your brief here that the interest rate is the most important thing, the thing which is of the greatest interest to you in this new Bank Act, in order that you may compete on more equal terms with near-banks. All this is designed, of course, to attract deposits, I believe that that is the main burden of your argument. That is why you would like that ceiling of 6 per cent removed. You would like to attract more deposits by having more interest. Where would you get these deposits? Would it be done to the detriment of the near-banks of which we have been speaking, among other things, finance companies, *Caisse populaires*, trust companies or what have you? Is that where you will find these deposits which you seem to lack at the present time?

(English)

Mr. PATON: The answer is yes. If the banks, by virtue of removal of the 6 per cent, can attract additional deposits that would come from other competing deposit-taking institutions.

(Translation)

Mr. COMTOIS: Now, Mr. Paton, do you believe that the improvements you have been requesting here in respect of the Bank Act—or those improvements which are suggested in the Bank Act—are such as to give you any comparative advantage over other institutions? Will this provide you with any marked advantage in order to obtain extra funds?

(English)

Mr. PATON: No sir, by virtue of this act we would not be attaining any competitive advantage; we would be eliminating the competitive disadvantage that we currently operate under.

(Translation)

Mr. COMTOIS: As you see, Mr. Paton, what happens is this. When we put money in the bank, when we make a deposit, this deposit, through the operations of the banking system, may engender a larger amount of credit. On the other hand the deposit made in a *Caisse populaire* or other such institution, cannot bring about an expansion in the credit, a reproductive phenomenon, if we may call it that.

(English)

Mr. PATON: That reproductive phenomenon is directly in the hands of the Governor of the Bank of Canada, who has the over-all control.

(Translation)

Mr. COMTOIS: But it is always based on deposits?

(English)

Mr. PATON: From my viewpoint and I think it is also the viewpoint of the other bankers, there is no difference between a deposit in a non-bank financial institution, as the Governor referred to it, and a bank.

(Translation)

Mr. COMTOIS: True, but if this deposit is put in a *Caisse Populaire*, for instance, the same phenomenon does not happen in those cases. What happens is quite different. The same thing does not happen. What I wanted to say is this: this bank deposit does not produce the same effects if it were put in a trust company or a *Caisse Populaire*. Is that true, or am I wrong?

Mr. LAVOIE: It is exactly the same thing in both instances. Whether a deposit is put in a *Caisse Populaire* or whether it is put in a bank, it is still a deposit. It cannot reproduce itself, as you claim.

Mr. COMTOIS: But to return to what I said a moment ago. If you put this deposit in a *Caisse*, eventually it returns to the bank, does it not? In the phenomenon we were discussing some time ago, Mr. MacIntosh explained the whole process. This deposit, which is put in the *Caisse*, or in another such institution, necessarily must return to the banking system, which allows for the circulation of credit and the multiplication of credit.

Mr. LAVOIE: But these deposits go from the *Caisse Populaire* to a bank, or conversely, they can go from a trust company to a bank, and so on.

Mr. COMTOIS: Yes, but what if these deposits remained with the *Caisse Populaire* without going back to the bank?

Mr. LAVOIE: In that case the *Caisse Populaire* could make loans. The more deposits there are in a *Caisse Populaire*, the more loans it can make.

Mr. COMTOIS: But can the same thing happen in both cases?

Mr. LAVOIE: You mean where?

Mr. COMTOIS: Within the *Caisse Populaire* system.

Mr. LAVOIE: Well, it is quite simple. You go and get deposits and then you make loans. It is exactly the same thing as with the banks.

Mr. CAQUETTE: Mr. Comtois, the Bank of Canada does not transact business with *Caisses Populaires*.

Mr. LAVOIE: That is a fact.

Mr. COMTOIS: It deals directly with chartered banks.

Mr. LAVOIE: Yes.

Mr. COMTOIS: It is what happens within the chartered banks which produces the credit to which reference was made.

Mr. LAVOIE: But I believe these two things are entirely different. A deposit in a *Caisse* or a deposit in a bank has exactly the same effects.

Mr. COMTOIS: Well why, then, do banks want to have deposits?

Mr. LAVOIE: Exactly for the same reason why the *Caisse Populaire* wants to attract deposits. It is exactly the same thing. The more deposits we have in a *Caisse Populaire*, the better it is for it. It is the same thing for the bank.

(English)

The CHAIRMAN: Order, please. May I suggest to the members of the committee that if they wish to consult with one another while the questioning is going

on that they try to do it in a moderate fashion in order that they will not interrupt the procedure.

(Translation)

Mr. COMTOIS: So, according to you there is no difference. This is merely a matter of competition. There is nothing intrinsically different from the point of view of deposits?

Mr. LAVOIE: I cannot see any.

Mr. COMTOIS: None at all?

Mr. LAVOIE: I cannot see any.

Mr. COMTOIS: A second question—

(English)

Mr. PATON: If I might interject, Mr. Comtois, one other reason for the issuance of debentures would also be an area in which, by virtue of the advantages of Bill No. C-222, we would be able to acquire funds to look after our loan demands, as well as deposits from the competing institutions. It is that other area which is included in the Bank Act that is referred to.

(Translation)

Mr. COMTOIS: Mr. Paton, could you tell me if the credit restrictions which we have been experiencing of late have been imposed by the Bank of Canada, or have they been imposed by the various chartered banks, for the purpose of having the 6 percent ceiling removed?

(English)

Mr. PATON: I can assure you most definitely that the chartered banks have had no part in suggesting the imposition of credit restraints for the purpose you mention. In fact, they have no part in imposing credit restraints, period.

(Translation)

Mr. COMTOIS: Is it simply the effect of the Bank of Canada policy which has brought this about?

(English)

Mr. PATON: I would say, Mr. Comtois, in fairness—and I do not pretend that I know, all I am not running for the governorship of the Bank of Canada—most definitely that it would be unfair to say that they have been following a credit restraint policy. The money supply has indeed increased. What has happened, with the buoyant economy we have had, is that the increased pressure of loan demands has exceeded the increase in the money supply that the Governor of the bank in his wisdom feels is best for the economy. So, it would not be fair to leave on the record that we feel that any policy of credit restraint is directly attributable to the Bank of Canada.

(Translation)

Mr. COMTOIS: But, Mr. Paton, is the Bank of Canada in a position to dictate policy to you under the present Act?



(English)

Mr. PATON: By virtue of their ability to control the reserves of money supply, yes. This is the manner in which. Through us, they control the money supply. They, in effect, decide what pool of funds is available for lending by all competing institutions.

(Translation)

Mr. COMTOIS: Still through the operation of the reserve system?

(English)

Mr. PATON: Through the chartered bank system by virtue of the reserves that we would carry with them.

(Translation)

Mr. COMTOIS: Now, Mr. Paton, with secondary reserves provided for under the new Act, will the Bank of Canada enjoy still more complete control over your activities?

(English)

Mr. PATON: I think the answer to that is yes. The indication is that the secondary reserve will be used on a stand-by basis and I think this is on the record. Notwithstanding that, the imposition of a statutory secondary reserve does put the ability and the legal power in the hands of the Bank of Canada to adjust the secondary reserve along the percentages shown in the act at so much per month, if the Governor so wishes.

(Translation)

Mr. COMTOIS: At that point, Mr. Paton, we are not dealing here with competition. It is the Bank of Canada's policy which will dictate your own policy to you.

(English)

Mr. PATON: It will dictate to the extent of the tools with which we have to do our job. The Bank of Canada has control over that. Now it will have, under the new act, even more control, in that it will be further accentuated by an imposition of a statutory secondary reserve, and we in the Association feel that this is not necessary.

Mr. COMTOIS: It would be harder for you to compete under this new system?

Mr. PATON: It could be an additional cost to us by forcing us to hold a larger percentage of our assets in the form of relatively low yielding securities.

(Translation)

Mr. COMTOIS: Mr. Paton, under their own Act Quebec savings banks are granted the privilege of making second mortgage loans. I do not think you enjoy that privilege under the Bank Act.

(English)

Mr. PATON: That is correct, sir.

Mr. COMTOIS: Would you like to have that one?

Mr. PATON: I would be well satisfied to work on the first mortgage loans if I had an opportunity to do so.

The CHAIRMAN: Mr. Paton, if I may interrupt, I believe Mr. Elderkin wishes to make a comment on what powers you are going to have under the new act with respect to mortgages. I think we should try and clear up this point. Mr. Comtois points out that the Quebec Savings Bank can take second mortgages. It was his understanding that a similar privilege was not to be accorded to the regular chartered banks. Mr. Elderkin commented that it is his understanding that the chartered banks will be able to take second mortgages provided the first and second mortgage total does not exceed a certain level. I thought it would be useful if we turned to the reference in the act.

Mr. ELDERKIN: Just a moment and I will try to find it.

Mr. PATON: I think it is clause 75(3), Mr. Elderkin.

The CHAIRMAN: It is page 52.

Mr. ELDERKIN: That is exactly the same as in the Quebec Savings Bank Act, Mr. Chairman, it collects the amount of the first mortgage.

The CHAIRMAN: Well, you cannot say you came here and did not go away with something that you did not expect!

Mr. PATON: That is true, Mr. Chairman.

(Translation)

Mr. COMTOIS: So, the chartered banks will be able to make second mortgage loans.

Mr. LAVOIE: Mr. Comtois, if you have a look at 75 (3) you will see that the banks will have a right to make mortgage loans as long as it does not go beyond 75 per cent of the value of property.

Mr. COMTOIS: There is no reference to first or second mortgages?

Mr. LAVOIE: No, simply that the total of loans may not exceed 75 per cent.

Mr. COMTOIS: Well, Mr. Lavoie, since I am discussing this matter with you, I would like to put a sample case to you to find out what is the feeling of the banks in this respect. Say a person holds a first mortgage of \$10,000 at 6 per cent and a second mortgage of \$5,000 at 15 per cent from a finance company. This party goes to the bank to ask for a \$15,000 first mortgage, shall we say at an 8 per cent interest. Will the competitor to which reference was made a while ago have any influence on that? Would you accept a mortgage of that type?

Mr. LAVOIE: If the mortgage does not go beyond 75 per cent of the value of the property, we could, I believe, grant that mortgage by paying off the two other mortgages.

Mr. COMTOIS: You could do it but as a matter of fact, will it happen?

Mr. LAVOIE: Well, it is difficult to give you an exact answer, I cannot really tell you what the banks will do in the future in this area, because we do not yet have that power, but I might say that we could make loans according to the National Housing Act. There was good cooperation from the banks and we did serve the population very well.

Mr. COMTOIS: But when we are speaking here of competition between one of your customers and an owner, will you take the interest of your customer at heart?

Mr. LAVOIE: Mr. Comtois, you understand that—

Mr. COMTOIS: There might be a conflict of interests?

Mr. LAVOIE: We are in business of course to make money. If somebody comes to us and asks for a mortgage loan, and if the proposal is good and if we have the necessary funds, I believe we will be able to deal with him.

Mr. COMTOIS: Even if it is to the detriment of one of your customers?

Mr. LAVOIE: It is rather difficult to say at this point what we will do if somebody has a first and second mortgage and he might like to convert it. He might go to a trust company, he might go to an insurance company, he might go to a *Caisse populaire*, he might go anywhere, to any organization which gives mortgage loans.

Mr. COMTOIS: But let us say that this possible customer will not automatically be refused because of that?

Mr. LAVOIE: I do not think so.

Mr. COMTOIS: I see.

(English)

Mr. FULTON: I have a question I would like to ask. Do the banks have their solicitors here? I think this question of whether clause 75(3) gives you the right to take second mortgages is quite a complicated legal question.

Mr. ELDERKIN: Mr. Fulton, may I suggest this was drafted by the Department of Justice on that very basis.

Mr. FULTON: I think before we assume it does that—

Mr. ELDERKIN: It has been in the Quebec Savings Bank Act.

Mr. FULTON: The Quebec Savings Banks Act does not extend to British Columbia. The question in my mind is whether clause 75(3) gives the banks the right to take second mortgages under British Columbia law.

The CHAIRMAN: I think your point is well taken. You are raising a question of just how for this section goes. May I suggest to Mr. Elderkin that he may wish to invite Mr. Ryan of the Department of Justice to come back and pay us another visit. Perhaps you could have him join with you in dealing with the extent of the section.

Mr. ELDERKIN: Yes.

Mr. PATON: Mr. Chairman, I might also add that our legal counsel is in attendance with us tonight and will be here tomorrow.

The CHAIRMAN: He so far has quite modestly refrained from joining the group of witnesses, but perhaps he may want to join you on Thursday for that purpose.

Mr. PATON: We will present this question at that time.

(Translation)

The CHAIRMAN: Do you still have any questions, Mr. Comtois?

Mr. COMTOIS: Yes, Mr. Chairman. The Bankers' Association seems to hesitate to accept the principle of limitation in buying into companies controlled by banks. Mention has been made of Roy-Nat which has been set up by a bank.



Now, could you tell me if these other aspects of banking activities cannot be explained by the need to get around the difficulties created by the Bank Act? You would like, say, to move into the mortgage market with its uncontrolled rates. But once this 6 per cent ceiling has been removed would these various companies remain necessary? Because, in actual fact, it was one way of getting around the Bank Act, was it not?

(English)

Mr. PATON: Mr. Comtois, I think possibly I might ask Mr. Coleman to reply to that because of his particular interest in one of the companies you mentioned.

Mr. COLEMAN: Well, the company you mentioned, Mr. Comtois, was set up by two banks and three trust companies. It was set up to serve an area which we felt was not being served by the chartered banks or other lending institutions at what we considered were reasonable rates of interest.

Mr. COMTOIS: In a field where the banks could not deal directly?

Mr. COLEMAN: That is correct. I might explain as a matter of information that Roy-Nat does not make loans, but buys securities of a corporation. I would say that there would be a place for that company to stay. I think the whole purpose of this bill is to encourage competition and I can see that even though we have an interest in that company, and if it is watered down to 10 per cent, as we hope it will not be, we would compete very freely with it. As I have said there are four other shareholders, and I think there will definitely be a field for it in the future.

Mr. COMTOIS: So you would like to continue in the same field, maybe with other kinds of companies?

Mr. COLEMAN: I would say yes, but probably the need to incorporate new companies will not be as urgent.

Mr. FULTON: Even under the amended law you as a bank would not be able to go into that field.

Mr. COLEMAN: Only up to 10 per cent ownership.

Mr. FULTON: As a bank you would not be able to operate in the field that Roy-Nat operates in even under this—

Mr. COLEMAN: Well, in some of the areas we would be able to, Mr. Fulton.

Mr. FULTON: Conveying mortgages.

Mr. COLEMAN: Yes.

The CHAIRMAN: Buying securities; you could not do that.

Mr. COLEMAN: Oh, yes. In most of the areas we would be able to do the same thing Roy-Nat does now.

Mr. FULTON: I will come back to that later.

Mr. LIND: Mr. Chairman, I have a supplementary question. What size of loan can Roy-Nat take?

Mr. COLEMAN: Would you like me to answer this? This is up to the directors, Mr. Lind.

Mr. LIND: Do you go under \$25,000?

Mr. COLEMAN: I think the minimum is \$25,000. This is up to the directors of the company.

(Translation)

Mr. COMTOIS: One last question, Mr. Chairman. Mr. Paton, do you believe that up to now near-banks, trust companies or mortgage companies, have taken risks which chartered banks could not or would not take?

(English)

Mr. PATON: They have been in a position to make loans at higher rates than chartered banks have, Mr. Comtois, and this might well have been accompanied by a willingness to take risks that chartered banks would not have taken. This would be a question of credit judgment, and of management judgment, on their part.

I think they most definitely have been in a position to take on higher risk loans than have the chartered banks.

Mr. COMTOIS: You could not take those risks because of the ceiling?

Mr. PATON: That is a contributing factor. Now, I would like to make definitely clear that our credit judgment would still apply, notwithstanding the existence or otherwise of the ceiling, but it is a fact that we could move into an area where there is a higher risk that would call for higher supervision, for more frequent investigation, perhaps more frequent statements in consideration of the account and this would enable us to take on these risks within our knowledge and our decision as to the credit worthiness of the customer.

The CHAIRMAN: The higher cost of servicing the loan. You take appropriate security precautions.

Mr. PATON: You take appropriate security as well with this new act. The answer would be that we could quite definitely move into a field of higher risk than we are in at present.

Mr. COMTOIS: Thank you.

The CHAIRMAN: Mr. More?

Mr. MORE (*Regina City*): Mr. Chairman, I might say that sitting with three privy councillors, one an accountant, and two lawyers, and one a banker of experience, I feel that I am really in. With Mr. Paton's permission I would like to ask Mr. Coleman, do you conceive the restrictions in the proposed bill would mean that Roy-Nat would be dissolved?

Mr. COLEMAN: No, I would hope not.

Mr. MORE (*Regina City*): It would have to be reorganized and you would have to adjust your interest.

Mr. COLEMAN: If the relevant clause limiting ownership of a bank to 10 per cent is passed, Mr. More, we would definitely have to dispose of our interest down to 10 per cent.

Mr. MORE (*Regina City*): But you feel that it would continue in its field?

Mr. COLEMAN: Well, I hope it would, and I expect that it would.

Mr. MORE (*Regina City*): Is there anything that would affect the interests of trust companies in Roy-Nat, though, under this legislation?

Mr. COLEMAN: Do you mean from a competitive standpoint?

Mr. MORE (*Regina City*): No. You now have two banks and three trust companies. They can enlarge their interest to take up what the bank has to dispose of?

Mr. COLEMAN: That is correct.

Mr. MORE (*Regina City*): I was just interested in a couple of things this afternoon. We got into the question of regional banks, and head offices, and what difference it made to loans, and so on. Mr. Paton, do banks allocate their resources to areas of Canada? Do they make an allocation of what they conceive as the available resources each year to what they contemplate to be the demand of an area?

Mr. PATON: They do not.

Mr. MORE (*Regina City*): Each area, then, is free to apply and the bank judges the applications on their merit? There is no ceiling on what may be put out in any given area of Canada?

Mr. PATON: The credit totals are seasonal, depending upon the particular area. At one time there might be a high need for credit in a certain area of Canada after paying down for instance, in the west when the grain crops come in. Their peak requirements are at a different season of the year, perhaps, than the British Columbia lumber industry, and so on. But no attempt is made to define, or ration, or allocate a certain percentage of credit to the area.

Mr. MORE (*Regina City*): Another point that interested me is that at one time there were quite a number of branches of banks, and then they withdrew and cut down and centralized. I saw this happen in Regina, but now if a building is put up there is some bank in the corner of it. They are opening branches high, wide and handsome, it seems. I take it the basic reason for this is an effort to compete for deposits, and to render a handy service, but mainly to compete for deposits?

Mr. PATON: It is a part of our continuing effort to serve the Canadian public and go where the public are and where industry is, and where there is a need for a bank. There are no statutory qualifications required in Canada for a bank to open new branches, as there are in some countries, and the banks compete aggressively for suitable areas for opening new locations.

Mr. MORE (*Regina City*): But it is for deposits. Would that not really be the basic reason that is involved in opening new branches?

Mr. PATON: I would say that there is nothing more acceptable to us today than deposits but, looking ahead and looking back, we have opened in areas where from time to time—and I hope we will get back to this—we can attract loans as well as deposits. At the present time the answer to your question is in the affirmative.

Mr. MORE (*Regina City*): If there are no deposits you are not going to be available for many loans. In regard to the proposals concerning the interest rate,



I understood this afternoon the first change will give you 7 per cent as an effective ceiling, rather than the present 6 per cent, under the proposed bill?

Mr. PATON: Yes. If the act were passed tomorrow I believe the effective rate that would apply from the July, August and September average yields on bonds would be 7 per cent, and if the effective date of passing were January 1st, it might be closer to  $7\frac{1}{4}$  per cent.

Mr. ELDERKIN: It depends on the six months ended May and November, as far as the interest rate maximum is concerned.

Mr. PATON: But the initial entry—

Mr. ELDERKIN: This will depend on the three months ended in November. It will take effect in January.

Mr. PATON: Was I not right in saying that if by chance it were passed tomorrow that you would go back? My purpose in getting it was to get those three months—

Mr. ELDERKIN: No, if it were passed tomorrow nothing would take effect until the first of January.

Mr. PATON: Oh yes, I see.

Mr. MORE (*Regina City*): As of the first of January it is conceivable, then, that you would have a ceiling of 7 per cent if the act were passed in its present form and, in the competition for deposits, by approximately how much would this new ceiling enable you to increase the interest on deposits? What would you envisage? You are paying 3 per cent now.

Mr. PATON: This is not a question that I can answer specifically, Mr. More. Somewhere in my study I had an amount savings interest increase that a percentage increase in the ceiling rate would permit, assuming that they were allowed to balance each other, but I am afraid that I cannot answer this question.

I would be inclined to say that the existence of a 7 per cent ceiling per se would not permit a very substantial increase in savings interest under current conditions.

Mr. MORE (*Regina City*): Then it would not make your competitive position for deposits one bit better than it is right now?

Mr. PATON: Our strong feeling is that the two-stage removal under current conditions of the ceiling is not in the best interests of the Canadian economy. We feel that the ceiling should be removed.

Mr. MORE (*Regina City*): In your opinion it is not a realistic approach to the present needs? Can I put it that bluntly? Will you accept that?

Mr. PATON: Yes, that is the point I wanted to make.

Mr. MORE (*Regina City*): If the interest rate were completely removed—and I would like initially to keep to the present deposits on which you are paying 3 per cent—what would you envisage as the general action of the banks in this area in competition with the near-banks, credit unions, and so on, for deposits. What would you conceive to be the first upward push with the situation as it is now?

Mr. PATON: And the ceiling completely removed?

Mr. MORE (*Regina City*): Yes.

Mr. PATON: In competition for deposits, the only effective way we can be successful would be to make our interest rate attractive or, alternatively, devise other methods of attracting deposits by creating new specific savings instruments.

Over the past few years particularly, when the interest rate on savings accounts itself has remained at 3 per cent, various banks have already evolved new deposit instruments, such as savings certificates, personal savings plans, deposit receipts, term deposits and bearer discount notes. They have already been using a fair amount of ingenuity in endeavouring to produce instruments of a special type and a special term on which we could pay rates that are sufficiently attractive for us to acquire deposits. I think removal of the ceiling would accentuate this, and in all probability—and once again I cannot speak for all the banks, because there will be no agreement regarding what one does with interest rates—the natural expectation one might have would be that the savings interest rate would be increased.

Mr. MORE (*Regina City*): You cannot speak for all the banks, but I think you said this afternoon that as a matter of course, because management was similar, and so forth, you would expect uniformity.

This does not hold true in the near-banks. Near-banks will pay  $5\frac{1}{4}$  per cent, some  $5\frac{1}{2}$  per cent; on other instruments you get  $6\frac{1}{4}$  per cent,  $6\frac{1}{2}$  per cent and  $6\frac{3}{4}$  per cent. I can name one that did this as of last week.

Mr. PATON: I think, Mr. More, these are on a different time basis. In certain cases there are guaranteed investment certificates; some are one year, two year, five year certificates. There is, indeed, a variety of rates, and you will also find in the banks at the moment that there is a variety of rates.

Mr. MORE (*Regina City*): Yes, 5 per cent for 90 days on Friday. I do not see how you can attract very much of that sort of money in competition at that rate. This is the point I am trying to make. I happen to be an executor of an estate with a considerable amount of money, and we had to make an investment last week. The bank rate was 5 per cent, and a little better in one case for 90 days, whereas you could get more than that from your competitors.

This is the point I am trying to make, and what I am really trying to find out is if the bank ceiling were removed and you had open competition, would you go to the present rates of your competitors to attract your deposits? There is nothing to stop them from moving up, and perhaps the field in which they operate would allow them to move up. Where does this leave the people who are seeking money to get it now, under compensating balances, and so on, from you cheaper than they can get it from these other sources? They face higher interest rates, do they not? I am not being critical of this. The point I am trying to make is that liquidity is such that this is just the nature of the times, and in the field you have no alternative if you are going to get deposits. Is this true?

Mr. PATON: If we are going to get deposits we have to compete, and we have to compete by making our offerings more attractive than we are able to do under present conditions.

Mr. MORE (*Regina City*): And you have to gain the deposits to have the money available to enter the new fields that you are being permitted to enter under the act. Is that not true? So that the passing of the act in itself does not open to the public any greater service from the bank unless they are able to attract greater deposits?

Mr. PATON: That is right, and our participation in these new areas eventually will average out and lower the average cost to the public, as it did in the personal loan field, for example, when we entered that.

This would apply in other areas of lending that we would be permitted to go into, and would be able to go into provided we have the money to do so. In effect there would be a levelling out of the average cost of borrowings to the Canadian public as a whole.

The CHAIRMAN: Mr. More, perhaps you might wish to complete your questioning on Thursday.

In order to keep our printed proceedings as clear as possible, I will ask the Committee to propose a motion that Mr. Hackett's very interesting paper tabled by Mr. Paton entitled "Cash Ratio Management—Proposed Twice Monthly Averaging Technique", and the comments of the association on the paper headed "Proposal for Deposit Insurance", which was also tabled today by Mr. Paton, be incorporated in our minutes for today.

Mr. MONTEITH: I so move.

Mr. LEBOE: I second the motion.

Motion agreed to.

The CHAIRMAN: Since we are agreed on that, I think that we should now adjourn.

(*Translation*)

Mr. GRÉGOIRE: I was asked a while ago to table the letters I sent to the bank presidents and the answers I got. Could I ask each of the gentlemen if they have any objection to that? This is done regularly in the House when we are speaking of the tabling of documents.

Mr. CLERMONT: I believe Mr. Grégoire did not ask their views on quoting certain paragraphs from these letters here.

Mr. GRÉGOIRE: To return to my question, will I be allowed to ask the gentlemen first? I believe that that would be more proper.

(*English*)

The CHAIRMAN: I think the reply is yours unless it is marked "confidential", but I have no objections to your confirming that the members of the Association wrote you in such an interesting manner. We would be pleased to have these letters part of our record.

Mr. CLERMONT: I will do that.

Mr. PATON: I might suggest, Mr. Gray, that the presidents of the banks who signed these letters are not permitted to be members of the Association. Members of the Association comprise the general managers of each bank.



The CHAIRMAN: In this case I will say silence means consent, and you have it, so the letters will be tabled pursuant to the motion.

Mr. FULTON: When will the steering committee meet? There is a question about next week. As you will appreciate, those sitting to your immediate left have a great problem with regard to Tuesday.

The CHAIRMAN: You have also caused problems for some of our witnesses, too. Thank you for raising this point. I wonder if the members of the steering committee could agree on a time to meet briefly tomorrow to review this?

Mr. MONTEITH: We all have caucus at 11 o'clock.

The CHAIRMAN: Yes, we are all in the same boat and I think I may have a luncheon meeting. The steering committee will meet right after orders of the day, otherwise we will inform you. In closing I will say, Mr. Grégoire—

*(Translation)*

—it is obvious that there are certain advantages to your position as an independent. The sitting is adjourned.

## Appendix J

October 24, 1966

SUBMISSION BY THE CANADIAN BANKERS' ASSOCIATION  
TO THE HOUSE OF COMMONS COMMITTEE  
ON FINANCE, TRADE AND ECONOMIC AFFAIRS  
REGARDING BILL C-222,  
AN ACT RESPECTING BANKS AND BANKING

The Canadian Bankers' Association welcomes the opportunity to present this brief outline of its views on some of the major matters related to Bills C-222 and C-190. We draw attention also to a few points of a technical character, which may be elaborated upon if the Committee so desires.

After the experience of the past year or two, there should be little need to emphasize the importance of Bill C-222 and the related proposals introduced by the Minister of Finance. All over the world, financial systems have been confronted by an unprecedented expansion of demands and by resulting upward pressures on the levels of interest rates. International competitive forces have continued to increase and the pace of technological advance has accelerated. In this environment, financial institutions cannot afford, any more than other businesses, simply to follow on blindly in old well-trodden paths. In the face of the growing and changing demands for financial services, in fact, the banks have reacted with a good deal of initiative and drive—so much so indeed that they have run increasingly up against legislative barriers that were framed in earlier different conditions. At the same time, other financial institutions have moved increasingly into what is essentially banking business, yet without being subject to the basic system of regulation and supervision established for banks. The need for legislative action to create more broadly competitive conditions has become all too apparent.

It has become the traditional practice in Canada to carry out a thorough review of the country's banking legislation and to renew the charters of the banks at 10-year intervals. It is therefore likely that whatever legislation is passed now will provide the basic ground-rules for the country's financial system for the next 10 years. This makes it even more important that the legislation continue and strengthen the essential safeguards for the public's financial savings while also providing needed adaptability and flexibility appropriate to a changing and challenging world.

The Bill which is now before the Committee has benefited from the work of the Royal Commission on Banking and Finance which issued its far-reaching report in the spring of 1964. The Bill also reflects a substantial recognition of the important financial developments of the ensuing period. Yet a number of fundamental questions remain. We trust that the discussions of the Committee will be helpful in clarifying these matters.

*Interest Rate Ceiling*

As the Finance Minister noted in his introduction of Bill C-222, both the Royal Commission on Banking and Finance and the Economic Council have recommended complete removal of the 6 per cent interest rate ceiling which applies only to loans made by the chartered banks and the Quebec Saving Banks and not to those made by any other institution or corporation. It is worth emphasizing, indeed, that the Commission's recommendation was that the ceiling should be eliminated, "regardless of other changes in the legislation" (p. 364).

As the basis for its recommendation, the Commission found that:

- (a) The 6 per cent ceiling "impedes the flow of credit to some borrowers and—by driving them to higher-cost lenders—frequently harms the very people it is designed to help" (p. 562).
- (b) More specifically, "the ceiling stands in the way of flexible lending by the banks in that it frequently prevents them from making loans on which higher rates must be charged to cover administrative costs and risks" (p. 364).
- (c) In consequence, the ceiling "discriminates against borrowers such as small businesses which, if they are to obtain funds at all, must turn to other lenders which charge rates well above those the banks would ask if free to do so". As the Commission points out, the limitations on the banks have the effect of "sheltering high-cost lenders from effective competition" (p. 365).
- (d) Because of the ceiling, "the chartered banks are unable to pay as high returns on their liabilities (i.e. deposits) as they otherwise might. Some savers are accordingly penalized, although others are able to obtain higher returns on their funds from unrestricted institutions which are direct competitors of the banks" (p. 562).
- (e) Finally, the Commission notes that "the distorting effects of the 6 per cent ceiling have been most acute in periods of credit restraint... At such times (the Banks) cannot compete equally for funds and thus have no choice but to resort to arbitrary rationing procedures in their lending" (p. 365).

Though accepting a substantial part of the Commission's arguments, the Government has concluded that the benefits in the way of a more satisfactory rationing of loans in the present period of exceptional demands for credit would not outweigh the uncertainties and fears that might be created by removal of the ceiling right in the midst of the period of strain. Thus, the Bill provides only for a moderate immediate relaxing of the ceiling and for eventual removal whenever interest rates in general fall back appreciably from recent levels. In our view, however, the need for a transitional arrangement is in itself quite dubious, and there is the further danger that heavy demands for credit might be sustained much longer than has been assumed, thus delaying or even preventing the move to what has been accepted as the desirable condition for the longer term.

In introducing Bill C-222 in July this year, the Finance Minister referred to the world-wide increases in interest rates which had occurred since the first revision bill was before the House a year earlier. In the period since July, this trend has been further extended, with the prime lending rate of United States



banks rising to 6 per cent, and other rates of course running above this. Rates in most overseas countries have also increased while in Canada the yield on long-term government bonds has risen to 5½ per cent or more with shorter-term yields running between 5 per cent and 6 per cent. In such circumstances, the existing ceiling for Canadian banks has become increasingly unrealistic, and even the proposed formula for interim relaxation would provide a degree of adjustment only after an appreciable time-lag.

Of even more significance, however, is the question of what kind of world economic and financial conditions are to be expected for the period ahead. Though there are obviously many uncertainties in the international picture, of both a political and economic character, the pressure for large military and aid expenditures seems bound to continue strong. World-wide demands for capital will also continue to be stimulated by the rapid pace of technological advance, by the heavy emphasis on space exploration, and by the growing needs for coping with the side-effects of growth in such areas as air and water pollution, urban redevelopment, and so on. At the same time, as the annual reports of the Economic Council have shown, the growth objectives appropriate to the present and prospective labour force expansion on this continent also imply high rates of industrial capital formation. In these circumstances, there is at least reason to doubt that interest rates will within a reasonably short time decline to the level required to trigger full removal of the 6 per cent ceiling. Yet if demands for capital over the coming years do run as strongly as has been suggested, it will be that much more important to have the recognized benefits of flexibility and competition in Canada's financial system.

For all of these reasons, the Association still holds to the view that unqualified removal of the ceiling is desirable in the best economic interests of the country.

### *Mortgage Lending*

The Canadian public undoubtedly welcomes the new provisions which will permit banks to become active sources of both N.H.A. and conventional mortgages. With respect to N.H.A. mortgages, the new provisions will remove the anomaly that now exists. The chartered banks since 1954 have been approved lenders under the Act and participated actively until they were effectively excluded when the rate on such mortgages, set by Order-in-Council, moved above the lending rate ceiling of the banks. Extension of powers to include conventional mortgages should greatly improve the whole structure of mortgage lending facilities.

In assessing the implications of the new arrangements, it is well to recognize that the extent of any bank's participation in the mortgage field will have to be determined in the light of the total resources at its disposal and of the demands on its resources for established areas of lending. As long as the current pressure of demands on real production capacity persists, the Bank of Canada could be expected to keep a tight rein on the total funds at the banks' disposal. In such circumstances it would not be helpful to anyone to build up unwarranted expectations as to the volume of new mortgage funds that can be provided in the relatively near term. However, participation by the banks should lead ultimately to a more competitive rate structure for mortgage loans especially in areas of the

country already served by banks but where institutional mortgage lenders are not represented. The banks quite naturally will be eager to make the most of their new powers for mortgage lending, and in the longer run the Canadian public is certain to benefit from the important contribution the banks will be making in this field of lending.

### *Debenture Financing*

The Association also welcomes the new provisions with respect to debenture financing as a desirable innovation in Canadian banking. The issuance of debentures is a recognized means of corporate financing and has come into extensive use by the United States banks in recent years.

### *Changes in Reserve Requirements*

The proposed gradual lowering of the cash reserves to be held against notice or term deposits (though not the raising of reserves against demand deposits) is in accord with the recommendations of the Porter Commission (p. 392). The effect should be to improve the capacity of the banks to compete for the increasingly important pools of term funds. The existing limitations in this area, together with the ceiling on bank lending rates but not on those of the so-called near-banks, have been major impediments to an equitable and efficient growth of Canada's financial system. Depositors also have borne some of the cost of the previous inequities of financial regulation, and should accordingly benefit from the improved competitive conditions which will now become possible.

The net effect of the new split reserve system is to lower the total amount of cash reserves which the banks are required to carry by an appreciable amount, but not to anything like the level which would be needed solely for the banks' own operational purposes. It must be emphasized that the only justification for legal reserve requirements advanced by central banks lies in the role that they play in central bank monetary control, and not in terms of satisfying the real liquidity needs of the banks or of protecting the interests of depositors. These latter needs can be met only from cash or quickly-cashable assets held in excess of the legal requirements, keeping in mind also that essential safeguards are being provided by the whole system of inspection and audit carried on by the banks themselves and by the Inspector General of Banks. If there were no legal reserve requirements the banks would still have to maintain some level of cash holdings for operational purposes. As the chartered banks are not paid any interest on their deposits with the central bank, now in excess of \$1 billion, any reserves required by statute in excess of actual operating needs, represents a continuing loss of earnings by the banks and a continuing element of discriminatory treatment relative to competing institutions not subject to legal reserve requirements.

The provisions for secondary reserve requirements (now for the first time proposed on a statutory basis) contain similar elements of discriminatory treatment. The argument advanced for such requirements is that they facilitate more direct response by the banks to changes in monetary policy. After examining this contention, however, the Royal Commission concluded that "We are not persuaded by the evidence before us that any legislative power to direct the



allocation of the institutions' funds is necessary. These are in the main emergency measures, and if the authorities' case is well founded, co-operation will be forthcoming" (p. 476). In the light of these observations, the Association remains of the view that statutory provision for secondary reserve requirements is neither necessary nor desirable.

Among the many technical considerations involved in the determination of reserve requirements, one that deserves attention is the fact that bank holdings of coinage which the average person would assume to be the most solid of cash are not in fact officially counted as cash in the hands of a bank. Thus, beyond the primary and secondary reserve requirements that have been noted here the Canadian banks hold a substantial amount of coinage in their tills which serves to meet obvious public needs but which brings the banks no return and is not even recognized as part of their cash reserves. Steps were taken in the United States in 1959 and 1960 to remedy a similar situation and permit the inclusion of coin in calculation of cash reserves. The Association urges that action now be taken in this country to count Canadian coinage as part of bank cash in the determination of reserve requirements. Calculation of the amount of coinage held could readily be made on the same Wednesday formula basis as now governs determination of note holdings.

A serious question also remains with respect to the new provision for fortnightly averaging, instead of the previous monthly averaging, in the formula for determination of cash reserves. The major point at issue is the fact that, in the view of bank officers responsible for the day-to-day cash management of their institutions, fortnightly averaging would provide no obvious advantages to central bank monetary control while in operations of the short-term money market it would have serious destabilizing effects. The problem essentially is that many of the payments flows that balance themselves out over the course of a month simply do not do so within periods of only two weeks. The Association would be pleased to furnish additional support for its views on this rather technical subject if the Committee so desires.

#### *Limitations on Bank Participation in Other Corporate Ventures*

Section 76 of Bill C-222 requires banks to dispose, before July 1, 1971, of any voting stock interest in excess of 10% that they may have in any Canadian company, or in any foreign concern which along with the bank could vote 10% of the shares of a Canadian company. If shares held by the bank acquire voting rights later, and so become excess shares, the bank must dispose of them within two years, and likewise if the bank otherwise acquires excess shares. The Minister of Finance may extend these deadlines but not by more than two years altogether.

Certain exceptions from these provisions are permitted, namely—shares acquired in settlement of a debt to the bank; shares of the Export Finance Corporation, which is a government-encouraged joint venture of the banks, dating from 1961; and finally, any shares in a "bank service corporation". Not exempted, therefore, could be some of the financial enterprises in which banks have taken part, and often supplied a key initiative, in recent years.



What has happened in practice is that from time to time important gaps have developed in our capital markets. With the rapidity of the country's growth and the greater complexity of business and consumer needs, certain financial requirements were not being adequately and effectively met. Efforts of the banks to meet these requirements often meant, in the existing circumstances, the necessity to participate in other financial enterprises. These developments also reflected a growing spirit of enterprise and initiative within the banking system. For example, some of the newer ventures in which banks have been taking an active or leading part provide services in the areas of mortgage and real estate finance and in developmental financing of various types, many of which were not available before. So long as such endeavours serve to provide added services to the public, and to increase rather than decrease effective competition, it is hard to see how it is in the best interests of the country either to penalize the past enterprise that has set them up or to prevent such ground-breaking initiatives in the future.

Even from the standpoint of the government's own direct interests, the Bill seems unnecessarily rigid. Though specific exception is made for bank participation in the Export Finance Corporation, an agency established for the meeting of certain national goals, no provision is made in Bill C-222 for any other possible venture of a similar kind.

In the light of these important considerations, the Association feels strongly that Bill C-222 should be made more flexible with respect to the permissible degree of bank participation in other financial ventures. One possibility would be to make the matter explicitly one of government discretion. Another alternative would be simply to delete the last seven words ("not exceeding two years in the aggregate") from Section 76 Subsection 5 of the Bill. The provision then would be that "The Minister may extend the time for the sale or disposal of any shares under this section for a further period or periods." Though such an arrangement might still have a dampening influence on desirable enterprise, it would at least leave scope for useful bank initiatives and a testing in actual practice of their net benefits to the national economy.

#### *Disclosure of Accumulated Appropriations for Losses on Loans and Investments*

Section 60(2)(c) of the proposed legislation will require for the first time the annual publication of reserves against losses on loans and investments in a form prescribed in Schedule P. The effect of this provision will be to require a bank to reveal not only its accumulated appropriations for losses, but also its losses on lending and investing from year to year.

With respect to losses the position of a bank is considerably different from that of other businesses. Because of the overwhelming size of their liabilities and assets in relation to the income of any one year a very small percentage loss on assets—less than one per cent—would completely wipe out the year's income of any Canadian bank, producing an overall net deficit. This possibility is provided against by the retention of reserves designed both to encourage bankers to assume greater risks by anticipating losses and to enable them to absorb losses when they occur.

In the past neither the amount of these reserves nor losses charged against them have been required to be disclosed. This practice has been regarded as necessary to avoid creating concern among bank depositors as to the stability of the institution holding their savings, and has been supported by many authorities, including several Ministers of Finance.

Regarding disclosure of inner reserves it must be remembered that they are, of course, disclosed to the Minister of Finance, who has specific responsibility for determining the amount which, in his opinion, is a reasonable appropriation for a bank to transfer to its inner reserves. Periodically the Minister of Finance issues the rules by which he makes this determination. In addition, in a statement made in 1944, the then Minister of Finance stressed the role in this matter of the shareholders' auditors and of the Inspector General of Banks. He stated that:

"... it is a responsibility of the shareholders' auditors and of the Inspector General of Banks to see not only that inner reserves are built up to the level of adequacy but also that they do not exceed this level."

In summary, the arguments previously advanced for the continued non-disclosure, except to the Inspector General and the Minister of Finance, of such losses and loss reserves are:

1. The ability and willingness of the banks to take risks on loans and investments are essential to economic growth, but enforced disclosure of losses may inhibit management from taking such risks.
2. The stability of the banks, and the confidence of depositors and the public in that stability, are essential to the health of the whole economy.

The Association is of the view that these arguments are as valid today as they were in the past. Suggestions for disclosure of accumulated reserves of banks appear to be a by-product of buoyant economic conditions; the danger lies not in good years but in periods of economic decline, when publication of losses could not only impair the competitive position of a particular bank but also reflect on the stability of the whole banking system. In fact, at the peak of a period of rapid economic growth the reserves might appear very high reflecting the fact that many of the loans on the books of a bank could involve losses during a subsequent period of less buoyant economic conditions. On the other hand, at the low point of a recession, the loans on the books might well involve fewer potential losses even though at this point the dollar total of the reserves could be much lower.

No other commercial or industrial company is placed in the position of being required to reveal annually the amount of losses suffered on trading in particular products, development of new products which fail, bad debts, etc. since these are considered to arise from normal business activities. It is most difficult to accept the proposed requirement that each bank publish losses arising from normal banking activities, and therefore of a comparable nature, where the results of disturbance to public confidence would be of immeasurably greater consequence.

APPENDIX "K"

House of Commons  
Canada

OTTAWA, August 11, 1966.

Mr. G. Arnold Hart, president,  
Bank of Montreal,  
129 St. James Street,  
Montreal, Que.

Dear Mr. Hart:

Enclosed herewith you will find a Royal Bank of Canada newsletter dated June 1966 and entitled: "Economic Trends and Topics". It deals with the part played by chartered banks and the Bank of Canada in our Canadian financial system.

I would like to know your answers to the following questions:

First: Are you prepared to subscribe unreservedly to everything set out in this publication?

Secondly: If not, on what points do you disagree with its contents?

I am sorry to put you to this trouble, but knowing that the matter is of great interest to you, I venture to ask for your opinion.

Thanking you in advance, I remain

Yours truly,

GILLES GRÉGOIRE, M.P.,  
Lapointe County

Letter sent to:

Royal Bank of Canada: Mr. Earle McLaughlin, president, Place Ville-Marie, Montreal, Que.

Bank of Montreal: Mr. G. Arnold Hart, president, 129 St. James Street, Montreal, Quebec.

Banque Canadienne nationale: Mr. Louis Hébert, president, Place d'Armes, Montreal, Quebec.

Toronto Dominion Bank: Mr. A. T. Lambert, president, King and Bay Streets, Toronto, Ont.

Banque Provinciale du Canada: J. -Ubaldo Boyer, president, 221 St. James Street, Montreal, Quebec.

Canadian Imperial Bank of Commerce: Mr. W. M. Currie, president, 25 King Street, Toronto, Ontario.

Bank of Nova Scotia: Mr. William Nicks, president, 44 King Street, Toronto, Ontario.



## LA BANQUE PROVINCIALE DU CANADA

J.-U. Boyer  
President

MONTREAL, August 16, 1966.

Mr. Gilles Grégoire, M.P.  
House of Commons,  
Ottawa,  
Ont.

Dear Mr. Grégoire:

I have looked at the brochure which you sent me, containing a report prepared by the Royal Bank, but after reading it I realize that it would be very difficult to answer simply yes or no.

As you are a customer of one of our Quebec branches, we would be very happy to see you and to discuss this question, and probably others as well, in a friendly atmosphere.

If this suggestion interests you, please contact me; it will be my pleasure to give you an appointment.

Sincerely,

J. U. Boyer

THE ROYAL BANK OF CANADA  
HEAD OFFICE—MONTREAL

W. Earle McLaughlin  
Chairman of the Board and President

September 8, 1966.

Mr. Gilles Grégoire, M.P.  
House of Commons  
Ottawa  
Ont.

Dear Sir:

In reference to your letter of August 2, I am very happy to send you herewith twelve French copies of the June publication entitled: "Economic Trends and Topics". Naturally, I agree entirely with this text. I hope that it will be useful to you.

Sincerely,

W. E. McLaughlin  
Chairman of the Board and President

BANK OF MONTREAL  
HEAD OFFICE

R. D. Mulholland  
Executive Vice President  
and Chief General Manager

Montreal 1, P.Q.  
129 St. James Street West  
August 31, 1966.

Dear Sir:

Here are the additional comments I promised you when I acknowledged receipt of your letter of August 11.

It seems to me that the pamphlet which was included with your letter should be read in the light of the definition of its purpose. As indicated on the first page, this purpose is "to explain as clearly and simply as possible. . . how bank deposits and the total supply of money are controlled by the Bank of Canada". Clearly, since the purpose in question was to describe the process in terms which the layman could understand, only the essential could be given and we cannot expect to find a detailed explanation of the reactions of the various forces which interact to produce the results described. The details of these points will probably be discussed thoroughly when the Bill to amend the Bank Act reaches Committee level. Nevertheless, considering its limited objective, I feel that the pamphlet explains fairly clearly the essential elements of the mechanism whereby the money supply, as officially defined, is controlled by the central bank.

Sincerely,

R. D. Mulholland  
Executive Vice-President

Mr. Gilles Grégoire, M.P.  
House of Commons  
Ottawa, Ont.

Banque Canadienne Nationale  
Place d'Armes—Montreal

Louis Hébert  
President

August 17, 1966.

Mr. Gilles Grégoire, M.P., Lapointe County  
House of Commons  
Ottawa, Canada.

Dear Mr. Grégoire:

In your letter of August 11, you ask my opinion on the contents of a bulletin published by the Economic Research Service of the Royal Bank of Canada.

I agree with the views expressed by the author of this document. The facts stated and the supporting explanatory tables are exact and clearly show the role which the Bank of Canada plays in the application of the country's financial

policy, a policy developed jointly with the federal authorities and dictated by economic circumstances, depending on whether the latter call for a tightening or an expansion of credit.

This pamphlet clearly demonstrates that the conditions regulating the financial situation in Canada are not controlled in any way by the chartered banks as such; rather, the latter are subject to the decisions of the Central Bank.

Sincerely yours,

Louis Hébert

CANADIAN IMPERIAL  
BANK OF COMMERCE  
HEAD OFFICE  
TORONTO, CANADA

M. A. Crowe  
Economic Adviser

August 24, 1966

Mr. Gilles Grégoire, M.P.  
House of Commons  
Ottawa, Canada.

Dear Mr. Grégoire:

In Mr. Currie's absence, the letter which you sent him, concerning a brochure published by the Royal Bank of Canada, was passed on to me. The description of the operations of the Bank of Canada in this brochure concerns the effects of those operations on the entire banking system rightly specifies that control of the process is in the hands of the Bank of Canada.

Sincerely yours,

M. A. Crowe

THE BANK OF NOVA SCOTIA  
General Office  
Toronto 1, Canada

Office of the Chairman of the Board  
and President

August 23, 1966.

Mr. Gilles Grégoire, M.P.  
Lapointe County  
House of Commons  
Ottawa

Dear Mr. Grégoire:

The bulletin published by the Royal Bank, entitled "How the Bank of Canada controls the money supply", attempts to define this important economic role in a very simple manner. Hence, the explanation which it gives is elementary; indeed, it resembles that found in most introductory treatises on banking.



The study of banking and finance is complex and difficult. However, we feel that the Royal Bank bulletin gives a precise description of the basic mechanism for the *creation of money*. You have probably noticed that it also includes a bibliography for the benefit of those who are interested in studying this question in more detail.

Very sincerely yours,

F.W. Nicks  
Chairman of the Board  
and President

BANK OF CANADA Ottawa 4

August 15, 1966.

Mr. Gilles Grégoire, M.P.  
Lapointe County,  
House of Commons, Ottawa (Ontario)

Dear Mr. Grégoire:

I have received your letter of August 11 and the Royal Bank newsletter which accompanied it.

I feel that the best way to answer your questions is to send you a copy of the briefs presented by the Bank of Canada to the Royal Commission on Banking and Finance, and to refer you in particular to paragraphs 39 and 40 on page 18, and to paragraphs 35 to 46, from page 35 to page 39. We attempted in those briefs to deal as precisely as possible with the effects of the Bank of Canada's operations on the money supply in Canada.

However, it should be pointed out that those passages, like the Royal Bank's article, deal with the position of the banks as a group; they do not necessarily apply to the position of one bank in particular. If, for one reason or another, the public is not interested in depositing a larger amount of money in one particular bank, financial policy can do nothing to increase deposits in that bank. It is the public's confidence in individual banks and the interest rates and services offered by them to their customers which determines each one's share of total deposits resulting from the policy of the central bank.

I hope that this information will be of service to you.

Sincerely yours,

L. Rasminsky

Minister of Finance

Canada

Ottawa, August 18, 1966.

Mr. Gilles Grégoire, M.P.  
House of Commons,  
Ottawa, Canada.

Dear Mr. Grégoire:

I have received your letter of August 11 as well as the enclosed brochure published by the Royal Bank of Canada.

In my opinion, this brochure succeeds in achieving the aim set out in the foreword, i.e. it gives a simple and clear description of the manner in which the Bank of Canada carries out its operations relative to the deposit liabilities of the chartered banks and the money supply of Canada.

Yours sincerely,

Mitchell Sharp.

The Royal Bank of Canada  
Economic Trends and Topics  
Economic Research Department

June 1966

#### HOW THE CANADIAN MONEY SUPPLY IS CONTROLLED BY THE BANK OF CANADA

With every decennial revision of the Bank Act, there is renewed discussion, much of it ill-informed, of the so-called "creation of credit" by the chartered banks. It is sometimes implied that the banks can increase or decrease the money supply at will merely by increasing or decreasing their loans and investments. In other words, as it is sometimes put, banks "create credit with the stroke of a pen." In this way, it is argued, banks "create deposits" which in turn form the greater (and most volatile) part of the nation's money supply.

In fact, bank deposits and the total money supply are controlled by the Bank of Canada; and the purpose of this issue of *Economic Trends and Topics* is to explain as clearly and simply as possible exactly how this is done. A schematic table, using figures taken from the example in the text, illustrates step by step the effect of a specific, but typical, Bank of Canada operation upon chartered bank deposits and hence upon the total money supply. The short bibliography at the end may be helpful to those who wish to pursue the subject further.

Enclosed in this issue of *Economic Trends and Topics* is a chronology of selected events affecting the current revision of the Bank Act. This is intended to serve as a handy guide to legislation, official announcements and appointments, and other matters affecting the current revision of banking legislation. For ease of reference the chronology has been printed on a separate sheet.

This is an attempt to explain, in plain English, the mechanics of money-supply control by the Bank of Canada. The money supply is a measure of the total amount of money in the country; and in Canada the money supply is officially defined as currency in the hands of the public plus the Canadian dollar deposits of the chartered banks. The Bank of Canada, an agent of the government, makes

the level of the money supply whatever it considers appropriate; and it does this through its power to control the level of chartered bank deposits, the major component of money supply.

Bank deposits are expanded when the banks buy securities or make loans, because the parties who sell securities to the banks, or get loans from them, deposit the proceeds with the banks. In other words, as a general rule, banks make loans and pay for securities not by issuing bundles of currency but by crediting the deposit accounts of the borrowers or sellers, thereby increasing total deposits. Bank deposits are contracted when loans are paid off, or when the banks sell securities, because the repaying borrowers, or the buyers of the securities, write cheques in favour of the banks thus authorizing the banks to debit their deposit accounts, thereby reducing total deposits. In short, it would appear that banks by buying securities or making loans cause deposits to rise and by selling securities or reducing loans cause deposits to fall.

But this is not the whole story. If it were, the "stroke of the pen" critic of the banks would have a case.

Whether banks will buy securities or sell securities or expand or contract their loans depends on how much cash or funds the banks themselves have. Banks, like other business organizations, require a certain amount of cash for working purposes. The amount of cash required by a bank is in an almost constant ratio to its deposits and this is also true of the cash required by all banks together relative to total deposits.

In Canada today the law, as laid down in the 1954 Bank Act, requires that this "cash ratio" be 8 per cent, which is higher than the banks themselves would keep. Hence, it is this legal cash ratio, not working needs, that sets the banks' cash requirements. This means that for every \$100 deposits on the books of the banks the banks require \$8 in cash. And when the banks have cash on hand barely equal to 8 per cent of their deposits, they cannot let their deposits rise, unless they can get more cash. And they will not let their deposits fall, as a result, say, of net loan repayments, since this would leave them with too much cash.

Cash is a non-earning asset, and excess cash means an unnecessary sacrifice of earning power. The banks will therefore use up any excess cash immediately by making loans or buying securities, thereby restoring the original level of deposits. Thus, if the banks have deposits outstanding of \$100 million and cash of \$8 million, the banks will not be in a position to let their deposits rise above \$100 million. Neither will they let deposits fall below \$100 million.

Therefore, it is the amount of cash the banks have that sets the level of bank deposits. This "bank cash" is mainly in the form of balances held by the banks with the Bank of Canada (the rest is "till money"—Bank of Canada notes held by the banks). The Bank of Canada can cause these balances to increase or decrease by buying or selling securities, and, therefore, the amount of bank cash at any time is under the direct control of the Bank of Canada.

Suppose, for example, that the Bank of Canada buys \$8 million of securities from the public. It issued Bank of Canada cheques in payment. The public





III. Banks Acquire Additional Loans and Securities of \$92 million Causing their Deposits to Increase by \$92 million

<i>Assets</i>		<i>Liabilities</i>	
<i>Assets</i>		<i>Liabilities</i>	
Bank of Canada notes.....	20	Deposits:	
Balances with Bank of Canada...	68	existing.....	1,008
		new.....	92
Bank cash.....	88		
Loans and securities:			
existing.....	920		
new.....	92		
	<u>1,100</u>		<u>1,100</u>

Cash ratio is restored to 8%

deposit these cheques with the chartered banks. Bank deposits rise by \$8 million and the banks return the Bank of Canada cheques to the Bank of Canada to increase their balances with the Bank of Canada by \$8 million. That is, the banks now have \$8 million more in cash and \$8 million more in deposits outstanding. If before this, the banks had cash of \$80 million, and deposits of \$1,000 million, they will now have cash of \$88 million (80 plus 8) and deposits of \$1,008 million (1,000 plus 8). The percentage of their deposits offset by cash exceeds 8 per cent.

The banks may now acquire \$92 million of additional loans and securities and their deposits will rise by \$92 million if all the proceeds from the loans and security sales are deposited with the banks. Bank deposits will then total \$1,100 million (1,008 plus 92) while the cash held by the banks will still be \$88 million. Thus cash held by the banks will again represent no more than 8 per cent of the deposits outstanding, which is the amount of cash the banks are required to hold to support that volume of deposits.

So, in this example, the purchase of \$8 million in securities by the Bank of Canada caused bank cash to increase by \$8 million and thereby caused bank deposits, and hence the money supply, to increase by a total of \$100 million.

If, in our example, the Bank of Canada had sold \$8 million of securities, instead of buying them, bank deposits and the money supply, would have fallen by \$100 million. In other words, the Bank of Canada by buying or selling securities can control the amount of cash held by the banking system and thereby cause bank deposits to assume whatever figure the Bank of Canada desires. It follows, therefore, that the money supply is controlled not by the banks, but exclusively by Bank of Canada action giving effect to the monetary policy of the day.



A CHRONOLOGY OF SELECTED EVENTS AFFECTING THE  
CURRENT BANK ACT REVISION IN CANADA

1961

*June 20*

In the budget speech, the Government, "having in mind...the fact that the Bank Act must undergo its regular decennial review in 1964", announces its intention "to appoint a royal commission to examine Canada's financial structure and institutions".

*July 24*

Mr. Rasminsky is appointed Governor of the Bank of Canada.

*October 18*

The Royal Commission on Banking and Finance is appointed.

1962

*March 12*

The Royal Commission on Banking and Finance begins public hearings.

*June 18*

A general election is held. A Progressive Conservative government is re-elected but without a clear majority.

*June 24*

An austerity program is announced to deal with the foreign exchange crisis that developed in the spring.

The Bank of Canada and the chartered banks are scheduled to appear before the Royal Commission on Banking and Finance. Their appearance is postponed, presumably because of the exchange crisis and austerity program.

*August 9*

Mr. Nowlan is appointed Minister of Finance to succeed Mr. Fleming.

1963

*January 9-14*

The Bank of Canada appears before the Royal Commission on Banking and Finance.

*January 15-18*

The chartered banks appear before the Royal Commission on Banking and Finance.

*January 22*

The Royal Commission on Banking and Finance ends public hearings.

*April 8*

A general election is held. A Liberal government is elected but without a clear majority.

April 23

Mr. Gordon is appointed Minister of Finance.

October 1

Controlling interest in The Mercantile Bank of Canada is acquired by the First National City Bank of New York.

December 21

Application for a charter for Bank of Western Canada is officially announced in *The Canada Gazette*.

1964

February 5

The Report of the Royal Commission on Banking and Finance is signed.

February 27

Bill S-6 to incorporate Bank of Western Canada is given first reading in the Senate. It contains provisions to limit total non-resident ownership to 10 per cent.

February 29

Application for a charter for Laurentide Bank of Canada is officially announced in *The Canada Gazette*.

March 7

Application for a charter for Bank of British Columbia is officially announced in *The Canada Gazette*.

March 24

Bill S-13 to incorporate Laurentide Bank of Canada is given first reading in the Senate. It contains provisions to limit total non-resident ownership to 10 per cent.

April 9

The Government gives notice of its intention to extend the Bank Act to July 1, 1965. (Extension receives Royal Assent on June 18, 1964).

April 24

Report of the Royal Commission on Banking and Finance is released.

May 13

Bill S-20 to incorporate Bank of British Columbia is given first reading in the Senate. It contains provisions to prohibit non-resident ownership completely.

September 22

Amendments to the Canadian Insurance Companies, Trust Companies, and Loan Companies Acts are announced in the House of Commons. They contain provisions to restrict total non-resident ownership to 25 per cent and individual non-resident ownership to 10 per cent. Similar provisions, effective as of September 23, 1964, are promised for the new Bank Act.

1965

*February 16*

The Minister of Finance announces that provisions, effective as of February 17, 1965, will be incorporated in the new Bank Act to restrict individual resident ownership of bank shares to 10 per cent, and to prohibit the ownership of bank shares by any government.

*May 6*

Bill C-102 to amend the Bank Act and Bill C-101 to amend the Bank of Canada Act are introduced in Parliament.

*June 8*

The Government gives notice of intention to extend the Bank Act a second time from July 1, 1965, to December 31, 1965 or, if Parliament does not sit for 20 days in December, to the sixtieth sitting day thereafter. (Extension receives Royal Assent on June 23, 1965.)

*June 17*

Atlantic Acceptance Corporation goes into receivership.

*July 9*

It is revealed that British Mortgage & Trust Co. held an undisclosed amount of Atlantic notes.

*July 27*

The Government of Ontario offers to guarantee a loan to keep British Mortgage solvent.

*August 31*

Submissions on Bill C-102 to the Standing Committee on Finance, Trade and Economic Affairs are due by this date.

*September 7*

A general election is called and Parliament is dissolved. Bills C-101 and C-102 die in committee.

*November 8*

The general election is held. A minority Liberal Government is re-elected.

*November 11*

Mr. Gordon resigns as Minister of Finance. Mr. Sharp is named Acting Minister of Finance.

*December 17*

Mr. Sharp is appointed Minister of Finance.

1966\*

*January 24*

A bill to extend the Bank Act a third time, to December 1, 1966, is introduced in the House of Commons. (Extension receives Royal Assent on March 31, 1966.) Legislation to revise the Bank Act is promised shortly.

\* Compiled up to June 15th



*February 7*

The membership of the Standing Committee on Finance, Trade and Economic Affairs is announced.

*May 30*

Bill C-190 to amend the Bank of Canada Act is introduced in the House of Commons.

*June 13*

During debate on second reading of Bill C-190 to amend the Bank of Canada Act, the Minister of Finance reveals that the new Bank Act will contain new provisions for cash and secondary reserves.

## SELECT BIBLIOGRAPHY

Bank of Canada, *Evidence of the Governor before the Royal Commission on Banking and Finance* (Ottawa: Bank of Canada, May 1964), Submission II, Section D, para. 29-46, pp. 122-6.

A simple explanation of how the Bank of Canada controls the money supply, including a good short description of the effect of Bank of Canada operations on chartered bank deposits.

Canada, *Report of the Royal Commission on Banking and Finance* (Ottawa: Queen's Printer, 1964), pp. 93-101, 109-12.

A general explanation of the expansion and contraction of credit, including the expansion and contraction of the money supply, and a more detailed description, illustrated with accounting examples, of the expansion of chartered-bank and near-bank assets.

Federal Reserve Bank of Chicago, *Modern Money Mechanics A Workbook on Deposits, Currency, and Bank Reserves* (Chicago: Federal Reserve Bank of Chicago, May 1961), pp. 6-13.

A good description, illustrated with balance-sheet examples, of the basic steps in the expansion and contraction of bank deposits.

Galbraith, J. A., *The Economics of Banking Operations: A Canadian Study* (Montreal: McGill University Press, 1963), pp. 464-76.

A more sophisticated explanation of bank expansion taking into account various complications that arise in practice, with reference to further sources.

Hackett, W. T. G., *A Background of Banking Theory* (Toronto: The Canadian Bankers' Association, 1945), pp. 13-17, 23-29.

An explanation of how the Bank of Canada increases or decreases the cash reserves of the chartered banks and a fairly detailed description, illustrated with balance-sheet examples, of how these changes in cash reserves affect the earning assets and deposit liabilities of the chartered banks.

O'Brien, J. W., *Canadian Money and Banking* (Toronto: McGraw-Hill, 1964), pp. 72-9.

A brief account, illustrated with balance-sheet examples, of how the sale and purchase of government securities by the Bank of Canada affects the deposits of the chartered banks.

APPENDIX "L"

EXHIBIT NO. 15

CHARTERED BANKS

TRUST COMPANIES IN CANADA HAVING DIRECTORS  
WHO ARE ALSO DIRECTORS OF CHARTERED BANKS  
AT MARCH 1, 1966

Bankers' Trust Company

Bank of Montreal—Pembroke, J.

Canada Permanent Trust Company

Bank of Montreal—MacAulay, J. A., McIntosh, D. A.

The Bank of Nova Scotia—Harris, W. C.

The Toronto-Dominion Bank—Carmichael, H. J., Gardiner, F. G., Gooderham, H. S., Hatch, H. C., Lambert, A. T., Mackenzie, C. F., Matthews, A. B., Osler, G. P., Savage, L. M., Wilding, T., Winspear, F. G.

Canadian Imperial Bank of Commerce—Bishop A. L., Cockshutt, C. G., Sale, R. M.

The Mercantile Bank of Canada—Tanner, E. H.

Canada Trust Co.

The Toronto-Dominion Bank—Jeffery, J.

The Provincial Bank of Canada—Chagnon, R.

Canadian Imperial Bank of Commerce—Clyne, Hon. J. V., Harvie, E. L., Ross, Hon. F. M.

The Royal Bank of Canada—Meighen, M. C. G.

The Mercantile Bank of Canada—Walford, A. E.

Crown Trust Co.

Bank of Montreal—Berkinshaw, R. C.

Canadian Imperial Bank of Commerce—Davis, N. M., Fairley, A. L. Jr., Horsey, J. W., Hunter, G. R., Leitch, J. D., McDougald, J. A., McIvor, G. H., McMartin, A. A., Monast, A., Notman, J. G., Thornbrough, A. A.

Eastern & Chartered Trust Co.

Bank of Montreal—Jones, J. H. M.

The Bank of Nova Scotia—Aird, J. B., Boyles, T. A., Bradfield, J. R., Jackman, H. R., Lowson, Sir Denys, McInnes, D., Wilson, C. N.

The Toronto-Dominion Bank—Smith, W. D.

The Royal Bank of Canada—MacKeen, J. C.

The Mercantile Bank of Canada—Borrie, W. J., Gélinas, Hon. L. P.

Guaranty Trust Co. of Canada

Banque Canadienne Nationale—Clermont, G. O.

International Trust Co.

The Mercantile Bank of Canada—Clifford, S. B., MacFadden, R. P., Rockefeller, J. S.

Investors Trust Co.

Canadian Imperial Bank of Commerce—Curry, P. D., Glassco, J. G., Peterson, T. O.

## Liffey Trust Co.

Bank of Montreal—Pembroke, J.

## Lincoln Trust &amp; Savings Co.

The Toronto-Dominion Bank—Carmichael, H. J.

## Montreal Trust Co.

Bank of Montreal—Allen, G. H., Crabtree, H. R.

The Toronto-Dominion Bank—Lank, H. H.

Canadian Imperial Bank of Commerce—Foster, Hon. G. B.

The Royal Bank of Canada—Ambridge, D. W., Atkinson, T. H., Breen, J. M., Burton, G. A., Christopher, A. B., Covert, F. M., Duquet, J. E. L., Fuller, J. A., McLaughlin, W. E., McMahon, F. M., Phillips, L., Simpson, M. O., Thomson, P. N., Webster, C. W., Welsford, H. G., Woodward, C. N.

Banque Canadienne Nationale—Brais, Hon. F. P.

## Morgan Trust Co.

Bank of Montreal—Morgan, J. B.

## National Trust Co. Ltd.

The Bank of Nova Scotia—Brown, F. B., McCarthy, J. L., Nicks, F. W., Sherman, F. H., Willmot, D. G.

The Toronto-Dominion Bank—Powell, K. A.

The Provincial Bank of Canada—Carsley, C. F.

Canadian Imperial Bank of Commerce—Barrington, J. D., Gill, E. C., Glasco, J. G., James, W. F., McKinnon, N. J., Morrow, G.

Banque Canadienne Nationale—Charron, A., St. Laurent, R.

## Nova Scotia Trust Co.

The Bank of Nova Scotia—Schwartz, W. H. C.

The Toronto-Dominion Bank—Sobey, F. H.

## Regent Trust Co.

Bank of Montreal—Sellers, G. H.

## Royal Trust Co.

Bank of Montreal—Arbuckle, W. A., Birks, H. G., Bourke, G. W., Brenan, R. B., Crump, N. R., Eadie, T. W., Gordon, G. B., Hynes, L., Ivey, R. G., Jensen, A. C., Kirkpatrick, W. S., McMaster, D. R., Mockridge, H. C. F., Pembroke, J., Rolland, L. G., Scully, V. W. T., Sellers, G. H., Smith, H. G.

The Toronto-Dominion Bank—Lapointe, L. A.

Canadian Imperial Bank of Commerce—Fox, P. M., Harris, J., Lang, H. J., Mackenzie, M. W., Marler, Hon. G. C.

The Royal Bank of Canada—McLagan, T. R., Penhale, A. L.

The Mercantile Bank of Canada—Mitchell, H. T.

## Royal Trust Co of Canada

Bank of Montreal—Pembroke, J.

## Royal Trust Co. (C.I.) Ltd.

Bank of Montreal—Pembroke, J.

## Sherbrooke Trust Co.

Banque Canadienne Nationale—Faribault, M.



- Société d'Administration et de Fiducie  
Bank of Montreal—Lechartier, B. M.  
The Provincial Bank of Canada—Bock, R., Brilliant, J., Martineau, Hon. G.,  
Simard, A.
- Société Nationale de Fiducie  
The Royal Bank of Canada—Dupuis, R.  
Banque Canadienne Nationale—Blain, J., Ouimet, H., Tourigny, A.
- Trust Général du Canada  
The Provincial Bank of Canada—Benoit, B., Massé, L.  
The Royal Bank of Canada—Desruisseaux, P.  
Banque Canadienne Nationale—Beauchemin, P., Chartré, M., Cousineau, A.,  
Donohue, G. T., Elie, G., Faribault, M., Raymond, J.
- Victoria & Grey Trust Co.  
Bank of Montreal—Frost, Hon. L. M.
- Waterloo Trust & Savings Co.  
Canadian Imperial Bank of Commerce—McCulloch, H. L.  
The Royal Bank of Canada—Pollock, C. A.

EXHIBIT NO. 16

CHARTERED BANKS

INSURANCE COMPANIES IN CANADA HAVING DIRECTORS  
WHO ARE ALSO DIRECTORS OF CHARTERED BANKS  
AT MARCH 1, 1966

- Acadia Insurance Co.  
The Royal Bank of Canada—Covert, F. M., MacKeen, J. C.
- Acadia Life Insurance  
The Royal Bank of Canada—MacKeen, J. C.
- Albion Insurance Co. of Canada  
The Provincial Bank of Canada—Bock, R.
- Alliance Cie Mutuelle d'Assurance Vie  
The Toronto-Dominion Bank—Lapointe, L. A., Plourde, G.  
The Provincial Bank of Canada—Brilliant, J., Brouillet, I., Martineau,  
Hon. G.  
Banque Canadienne Nationale—Brais, Hon. F. P., Chartré, M.
- Allstate Insurance Co. of Canada  
Canadian Imperial Bank of Commerce—Burton, E. G.
- Allstate Life Insurance Co. of Canada  
Canadian Imperial Bank of Commerce—Burton, E. G.
- Arkwright Mutual Insurance Co.  
The Royal Bank of Canada—Simpson, M. O.
- Assurance-Vie du Saint-Laurent  
Banque Canadienne Nationale—Ferron, H.

- Atlas Assurance Co. Ltd.  
Bank of Montreal—Bienvenu, P.
- Aviation Insurance Agency (Canada) Ltd.  
Bank of Montreal—McIntosh, D. A.
- Beaver Insurance Co.  
Canadian Imperial Bank of Commerce—Thomson, H. W.
- British America Assurance Co.  
Bank of Montreal—Gordon, G. B., Smith, H. G.  
Canadian Imperial Bank of Commerce—Davidson, I. D., McKinnon, N. J.,  
Morrow, G.  
The Royal Bank of Canada—Dupuis, R.
- British Canadian Insurance Co.  
The Bank of Nova Scotia—McCarthy, J. L.  
Canadian Imperial Bank of Commerce—Davidson, I. D., Morrow, G.
- British Empire Assurance Co.  
The Bank of Nova Scotia—McCarthy, J. L.  
Canadian Imperial Bank of Commerce—Davidson, I. D., Morrow, G.
- Caledonian-Canadian Insurance Co.  
Canadian Imperial Bank of Commerce—Stewart, J.  
The Royal Bank of Canada—Keefer, R. H.  
Banque Canadienne Nationale—De Serres, R.
- Canada Life Assurance Co.  
Bank of Montreal—Davis, N. V., Frost, Hon. L. M.  
The Bank of Nova Scotia—Courtois, E. J., McCarthy, J. L., Nicks, F. W.  
The Toronto-Dominion Bank—Ashforth, A. C., Gordon, J. R.  
Canadian Imperial Bank of Commerce—Gill, E. G., Leitch, J. D., McKinnon,  
N. J.  
The Royal Bank of Canada—Dupuis, R.
- Canadian General Insurance Co.  
Bank of Montreal—Ivey, R. G.  
The Royal Bank of Canada—Webster, C. W.
- Canadian Indemnity Co. Ltd.  
The Bank of Nova Scotia—Smith, C. G.  
Canadian Imperial Bank of Commerce—Richardson, J. A.  
The Royal Bank of Canada—Riley, W. C.
- Canadian Pioneer Insurance Co.  
Canadian Imperial Bank of Commerce—Boyd, J. A.
- Canadian Premier Life Insurance Co.  
The Mercantile Bank of Canada—Benham, H. A.
- Canadian Provincial Insurance Co.  
Bank of Montreal—McIntosh, D. A.
- Canadian Reassurance Co.  
The Provincial Bank of Canada—Dionne, P. A.
- Canadian Reciprocal Insurers (Toronto)  
The Mercantile Bank of Canada—Walford, A. E.

Canadian Surety Co. Ltd.

Bank of Montreal—Sheppard, G. H.

The Toronto-Dominion Bank—Elliott, C. J., Lawson, H. H., Osler, G. P.

Car & General Insurance Corp. Ltd.

Bank of Montreal—Jensen, A. C.

Casualty Co. of Canada

The Toronto-Dominion Bank—Gooderham, H. S., Savage, L. M.

Casualty Insurance Co. of Canada

The Bank of Nova Scotia—Jackman, H. R.

Charter Oak Fire Insurance Co.

Canadian Imperial Bank of Commerce—Foster, Hon. G. B.

Coastal Insurance Ltd.

The Bank of Nova Scotia—Jodrey, J. J.

Commercial Life Assurance Co. of Canada

Canadian Imperial Bank of Commerce—Richardson, J. E.

Commercial Union—North British Group of Insurance Companies

Bank of Montreal—Crabtree, H. R., Pembroke, J.

The Toronto-Dominion Bank—Lapointe, L. A.

The Royal Bank of Canada—Wood, E. C.

Cie d'Assurance Canadienne Mercantile

The Provincial Bank of Canada—Benoit, M., Massé, L.

Banque Canadienne Nationale—Faribault, M.

Cie d'Assurance Canadienne Nationale

The Provincial Bank of Canada—Benoit, B., Massé, L.

Banque Canadienne Nationale—Faribault, M.

Cie d'Assurance Générale du Commerce

The Provincial Bank of Canada—Benoit, B., Massé, L.

Banque Canadienne Nationale—Faribault, M., Ferron, H.

Cie Mutuelle d'Assurance-Vie de Québec

Banque Canadienne Nationale—Cousineau, A., Tourigny, A.

Confederation Life Association

Bank of Montreal—McIntosh, D.A., Mockridge, H.C.F.

The Toronto-Dominion Bank—De Young, H. G., Harding, C. M.

Canadian Imperial Bank of Commerce—Black, G. M., Monast, A., Wadsworth, J. P. R.

The Royal Bank of Canada—Simpson, M. O.

Continental Insurance Co.

The Toronto-Dominion Bank—Lambert, A. T.

Crown Life Insurance Co.

Bank of Montreal—Jones, J. H. M.

The Bank of Nova Scotia—Lowson, Sir Denys, Sherman, F. H., Wilmot, D. G.

The Provincial Bank of Canada—Boyer, J. U.



- Dominion of Canada General Insurance Co.  
The Bank of Nova Scotia—Jackman, H. R.  
The Toronto-Dominion Bank—Gooderham, H. S., Savage, L. M.
- Dominion Insurance Corp.  
The Toronto-Dominion Bank—Lambert, A. T.
- Dominion Life Assurance Co.  
Canadian Imperial Bank of Commerce—Cockshutt, C. G.  
The Royal Bank of Canada—Pollock, C. A.
- Eaton Life Assurance Co., The T.  
Bank of Montreal—Kinnear, D.  
The Toronto-Dominion Bank—Jenkins, J. R.
- Empire Life Insurance Co.  
The Bank of Nova Scotia—Jackman, H. R.
- Excelsior Life Insurance Co.  
The Toronto-Dominion Bank—Gooderham, H. S., Mackenzie, C. F., Matthews, A. B.  
Canadian Imperial Bank of Commerce—Barrington, J. D.  
The Mercantile Bank of Canada—Walford, A. E.
- Export Credits Insurance Corp.  
The Royal Bank of Canada—Mannix, F. C.
- Federal Fire Insurance Co.  
Canadian Imperial Bank of Commerce—Cooper, R. W.
- Fire Insurance Co. of Canada  
Bank of Montreal—Bienvenu, P.
- General Accident Assurance Co. of Canada  
The Bank of Nova Scotia—Proctor, J. S.  
Canadian Imperial Bank of Commerce—Baillie, A. W., Currie, W. M.
- General Reinsurance Corp.  
The Royal Bank of Canada—Fuller, J. A.
- Global General Insurance Co.  
The Mercantile Bank of Canada—Gélinas, Hon. L. P.
- Global Life Insurance Co.  
The Mercantile Bank Of Canada—Gélinas, Hon. L. P.
- Global Reinsurance Co.  
The Mercantile Bank of Canada—Gélinas, Hon. L. P.
- Globe Indemnity Co. of Canada  
Bank of Montreal—Gordon, G. B., Smith, H. G.  
Canadian Imperial Bank of Commerce—Morrow, H.  
The Royal Bank of Canada—Dupuis, R.
- Gore District Mutual Fire Insurance Co.  
Canadian Imperial Bank of Commerce—Cockshutt, C. G., McCulloch, H. L.
- Grain Insurance Brokers Ltd.  
Bank of Montreal—Leach, A. S.

Grain Insurance & Guarantee Co.

Bank of Montreal—Leach, A. S., Sellers, G. H.

Great Eastern Insurance Co.

The Royal Bank of Canada—Webster, C. W.

Great West Life Assurance Co.

Bank of Montreal—Foley, H.S., Leach, A.S., MacAulay, J.A.

The Provincial Bank of Canada—Bélanger, M.

Canadian Imperial Bank of Commerce—Harris, J., Sale, R. M., Walker, W. P.

The Royal Bank of Canada—Riley, W. C.

Guarantee Co. of North America

Bank of Montreal—Gordon, G. B.

The Toronto-Dominion Bank—Cumming, A. A.

Guardian Insurance Co. of Canada

Canadian Imperial Bank of Commerce—Stewart, J.

The Royal Bank of Canada—Keefer, R. H.

Banque Canadienne Nationale—De Serres, Y.

Guildhall Insurance Co. of Canada

The Royal Bank of Canada—McLaughlin, W. E., Meighen, M. C. G.

Banque Canadienne Nationale—Brais, Hon. F. P.

Halifax Insurance Co. Ltd.

Canadian Imperial Bank of Commerce—Richardson, J. E.

Hudson Bay Insurance Co.

Bank of Montreal—Gordon, G. B., Smith, H. G.

Canadian Imperial Bank of Commerce—Morrow, G.

The Royal Bank of Canada—Dupuis, R.

Imperial Guarantee Accident Insurance Co. of Canada

The Bank of Nova Scotia—McCarthy, J.L.

Canadian Imperial Bank of Commerce—Davidson, I. D., Morrow, G.

Imperial Life Assurance Co. of Canada

Bank of Montreal—Sheppard, G. H.

The Bank of Nova Scotia—Harris, W. C.

The Toronto-Dominion Bank—Smith, W. D.

Canadian Imperial Bank of Commerce—Currie, W. M., Mackenzie, M. W.,  
Morrow, G., Stewart, J.

Banque Canadienne Nationale—St. Laurent, R.

Independent Insurance Managers Ltd.

Bank of Montreal—McIntosh, D. A.

Industrielle Cie d'Assurance sur la Vie

The Provincial Bank of Canada—Carsley, C. F., Massé, L.

Banque Canadienne Nationale—Charron, A.

L'Economie Mutuelle d'Assurance

Banque Canadienne Nationale—Faribault, M., ouimet, H.

Life Insurance Co. of Alberta

The Toronto-Dominion Bank—Winspear, F. G.

- Liverpool & London & Globe Insurance Co. Ltd.  
Bank of Montreal—Gordon, G. B.
- Liverpool-Manitoba Assurance Co.  
Bank of Montreal—Gordon, G. B.
- London Assurance, The  
Banque Canadienne Nationale—Brais, Hon. F. P.
- London & County Insurance Co. Ltd.  
Banque Canadienne Nationale—Brais, Hon. F. P.
- London Life Insurance Co.  
The Toronto-Dominion Bank—Jeffrey, J., Lambert, A. T.
- London & Lancashire Guarantee & Accident Co. of Canada  
Canadian Imperial Bank of Commerce—Morrow, G.
- Manufacturers Life Insurance Co.  
Canadian Imperial Bank of Commerce—Glassco, J. G.  
The Mercantile Bank of Canada—Seedhouse, A. T.
- Maritime Life Assurance Co.  
Bank of Montreal—Cook, E.  
The Bank of Nova Scotia—McInnes, D., Schwartz, W. H. C.
- Mercantile & General Reinsurance Co. of Canada Ltd.  
Bank of Montreal—Ash, W. M. V.
- Merit Insurance Co.  
Banque Canadienne Nationale—St. Laurent, R.
- Monarch Life Assurance Co.  
The Bank of Nova Scotia—Smith, C. G.  
The Toronto-Dominion Bank—Powell, K. A.
- Montreal Life Insurance Co.  
Bank of Montreal—Morgan, J. B.  
The Provincial Bank of Canada—Renaud, Hon. J. O.  
The Royal Bank of Canada—Phillips, L.
- Morgan Insurance Services Ltd.  
Bank of Montreal—Morgan, J. B.
- Mortgage Insurance Co. of Canada  
The Bank of Nova Scotia—Nicks, F. W.  
The Provincial Bank of Canada—van den Berg, G. J.
- Motor Union Insurance Co. Ltd.  
Bank of Montreal—Jensen, A. C.
- Munich Reinsurance Co. of Canada  
Bank of Montreal—Rolland, L. G.  
The Royal Bank of Canada—Atkinson, T. H.
- Mutual Life Assurance Co. of Canada  
Bank of Montreal—Berkshaw, R. C., Crump, N.R., Gordon, G. B., Pearson, H. J. S.  
The Bank of Nova Scotia—Proctor, J. S., Rea W. G.



- Canadian Imperial Bank of Commerce—Cooper, R. W., McCulloch, H. L.,  
Turner, H. M.  
The Mercantile Bank of Canada—Côté, P.
- National Fire & Casualty Insurance Co. Ltd.  
Banque Canadienne Nationale—Donohue, G. T.  
The Mercantile Bank of Canada—Gélinas, Hon. L. P.
- National Life Assurance Co. of Canada  
The Bank of Nova Scotia—Aird, J. B.  
Canadian Imperial Bank of Commerce—Thomson, H. W.
- Newfoundland Fire & General Insurance Co. Ltd.  
Canadian Imperial Bank of Commerce—Hickman, E. L.
- North American Life Assurance Co.  
The Bank of Nova Scotia—Brown, F. B.  
The Toronto-Dominion Bank—Elliott, C. J., Osler, G. P.  
Canadian Imperial Bank of Commerce—Mackersy, L. S.  
The Royal Bank of Canada—Breen, J. M.
- North American Life & Casualty Co.  
Canadian Imperial Bank of Commerce—Peterson, T. O.
- Northern Life Assurance Co. of Canada  
Bank of Montreal—Ivey, R. G.
- Norwich Union Fire Insurance Society Ltd.  
Canadian Imperial Bank of Commerce—Borden, H.
- Norwich Union Life Insurance Society  
Canadian Imperial Bank of Commerce—Borden, H.
- Pacific Coast Fire Insurance Co.  
Canadian Imperial Bank of Commerce—Buchanan, J. M.
- Paix Cie d'Assurances Générales, La  
Banque Canadienne Nationale—Chartré, M.
- Pilot Insurance Co.  
Canadian Imperial Bank of Commerce—Wadsworth, J. P. R.
- Planet Assurance Co. Ltd.  
Banque Canadienne Nationale—Brais, Hon. F. P.
- Pool Insurance Co. Ltd.  
The Royal Bank of Canada—Gibbings, C. W.
- Prévoyance Cie d'Assurance, La  
The Provincial Bank of Canada—Bock, R., Turmel, A.  
Banque Canadienne Nationale—Bherer, W., Charron, A., Crévier, E., Fari-  
bault, M., Raymond, J.
- Prévoyants du Canada, Les  
Bank of Montreal—Bienvenu, P., Lechartier, B. M.
- Quebec Assurance Co.  
The Royal Bank of Canada—Dupuis, R.
- Royal Exchange Assurance  
Bank of Montreal—Bienvenu, P., Lechartier, B. M.

- Royal Exchange—Atlas Group  
Bank of Montreal—Jensen, A. C., Morgan, J. B.
- Royal General Insurance Co. of Canada  
The Toronto-Dominion Bank—Winspear, F. G.  
The Royal Bank of Canada—Beaupré, T. N.
- Royal Insurance Co. Ltd.  
Bank of Montreal—Smith, H. G.
- Scottish-Canadian Assurance Corp.  
The Bank of Nova Scotia—Proctor, J. S.  
Canadian Imperial Bank of Commerce—Baillie, A. W., Currie, W. M.
- Seaboard Insurance Co. Ltd.  
The Royal Bank of Canada—Christopher, A. B.
- Société Nationale d'Assurances contre l'Incendie  
The Provincial Bank of Canada—Renaud, Hon. J. O.  
Banque Canadienne Nationale—Cousineau, A., Ouimet, H., Tourigny, A.
- Sovereign Life Assurance Co. of Canada  
The Toronto-Dominion Bank—Gardiner, F. G.
- Stability Life Insurance Co.  
The Provincial Bank of Canada—Dionne, P. A.
- Standard Life Assurance Co.  
Bank of Montreal—Arbuckle, W. A., Jensen, A. C., McMaster, D. R., Mul-  
holland, R. D., Rolland, L. G.  
The Royal Bank of Canada—Penhale, A. L.
- Standstead & Sherbrooke Insurance Co.  
Bank of Montreal—Crabtree, H. R.  
The Royal Bank of Canada—Penhale, A. L.
- Sterling Insurance Co. of Canada  
The Royal Bank of Canada—Penhale, A. L.
- Sun Alliance & London Insurance Group  
Banque Canadienne Nationale—Brais, Hon. F. P.
- Sun Insurance Office Ltd.  
Banque Canadienne Nationale—Brais, Hon. F. P.
- Sun Life Assurance Co. of Canada  
Bank of Montreal—Bourke, G. W., Crabtree, H. R., Molson, H. de M.  
Scully, V. W., Sinclair, Hon. J., Hart, G. A. R.  
The Toronto-Dominion Bank—Lank, H. H.  
Canadian Imperial Bank of Commerce—Smith, J. H.  
The Royal Bank of Canada—Covert, F. M., Fuller, J. A., Webster, C. W.  
Banque Canadienne Nationale—Brais, Hon. F. P., Hébert, L.
- Toronto General Insurance Co.  
Bank of Montreal—Ivey, R. G.  
The Royal Bank of Canada—Webster, C. W.
- Traders General Insurance Co.  
Bank of Montreal—Ivey, R. G.  
The Royal Bank of Canada—Webster, C. W.

- Travelers Fire Insurance Co.  
Canadian Imperial Bank of Commerce—Foster, Hon. G. B.
- Travelers Indemnity Co.  
Canadian Imperial Bank of Commerce—Foster, Hon. G. B.
- Travelers Life Insurance Co.  
Canadian Imperial Bank of Commerce—Foster, Hon. G. B.
- United British Insurance Co. Ltd.  
Bank of Montreal—Jensen, A. C.
- United Canada Insurance Co.  
Bank of Montreal—Jensen, A. C., Lechartier, B. M., Morgan, J. B.
- Western Assurance Co.  
Bank of Montreal—Gordon, G. B., Smith, H. G.  
The Bank of Nova Scotia—McCarthy, J. L.  
Canadian Imperial Bank of Commerce—Davidson, I. D., McKinnon, N. J.,  
Morrow, G.  
The Royal Bank of Canada—Dupuis, R.
- Western British America Assurance Companies Group  
Bank of Montreal—Hart, G. A. R.
- Western Surety Co.  
The Bank of Nova Scotia—Kramer, R. A.
- Westminster Fire Office  
Banque Canadienne Nationale—Braiss, Hon. F. P.
- Westmount Life Insurance Co. Ltd.  
Bank of Montreal—Allen, G. H.  
Canadian Imperial Bank of Commerce—Notman, J. G.  
The Royal Bank of Canada—Desruisseaux, P.

#### EXHIBIT NO. 17

#### CHARTERED BANKS

#### LOAN COMPANIES IN CANADA HAVING DIRECTORS WHO ARE ALSO DIRECTORS OF CHARTERED BANKS AT MARCH 1, 1966

- Administration & Finance Inc.  
The Toronto-Dominion Bank—Plourde, G.
- Admiral Acceptance Corp. Ltd.  
Canadian Imperial Bank of Commerce—Davis, N. M.
- Associated Finance Corp.  
Canadian Imperial Bank of Commerce—Notman, J. G.  
The Royal Bank of Canada—Duquet, J. E. L.
- Canada Permanent Mortgage Corp.  
Bank of Montreal—MacAulay, J. A., McIntosh, D. A.  
The Bank of Nova Scotia—Harris, W. C.



- The Toronto-Dominion Bank—Gardiner, F. G., Gooderham H. S., Lambert, A. T., Mackenzie, C. F., Matthews, A. B., Savage, L. M.  
Canadian Imperial Bank of Commerce—Bishop A. L., Burton, E. G.
- Canadian First Mortgage Corp.  
The Toronto-Dominion Bank—Osler, G. P., Wilding, T.
- Charter Credit Corp.  
The Toronto-Dominion Bank—Plourde, G.
- Colonial Finance Corp. Ltd.  
Canadian Imperial Bank of Commerce—Hermant, S.
- Colonial Finance Corp. (Hamilton) Ltd.  
Canadian Imperial Bank of Commerce—Hermant, S.
- Colonial Finance Corp. (Peterborough) Ltd.  
Canadian Imperial Bank of Commerce—Hermant, S.
- Combined Mortgage Corp.  
Bank of Montreal—Morgan, J. B.
- Crédit Adanac, Corp. de  
The Provincial Bank of Canada—Massé, L.
- Crédit Concorde Inc.  
The Provincial Bank of Canada—Brillant, J.
- Crédit Foncier Franco Canadien  
Bank of Montreal—Bienvenu, P., Lechartier, B. M.  
The Toronto-Dominion Bank—Lank, H. H.  
Banque Canadienne Nationale—Faribault, M.
- Crédit M-G Inc.  
The Provincial Bank of Canada—Dionne, P. A.  
Banque Canadienne Nationale—Ouimet, H., Tourigny, A.
- Crédit St. Laurent Inc.  
The Provincial Bank of Canada—Benoit, B.  
Banque Canadienne Nationale—Bherer, W.
- Eastern Canada Savings & Loan Co.  
The Royal Bank of Canada—MacKeen, J. C.
- Eaton Acceptance Co. Ltd., The T.  
Bank of Montreal—Kinnear, D.  
The Toronto-Dominion Bank—Jenkins, J. R. Wotherspoon, G. D. de S.
- Export Finance Corp. of Canada Ltd.  
The Bank of Nova Scotia—Boyles, T. A.  
The Provincial Bank of Canada—Lavoie, L.
- Fairway Finance Corp. Ltd.  
Canadian Imperial Bank of Commerce—Hermant, S.
- First National Mortgage (1962) Co. Ltd.  
The Mercantile Bank of Canada—Borrie, W. J.
- Genelco Finance Ltd.  
Canadian Imperial Bank of Commerce—Smith, J. H.

- General Mortgage Service Corp. of Canada  
The Royal Bank of Canada—Covert, F.M.  
The Mercantile Bank of Canada—Gélinas, Hon. L. P.
- Georgia Mortgages Ltd.  
The Bank of Nova Scotia—Brown, F. B.
- Hudson's Bay Co. Acceptance Ltd.  
Canadian Imperial Bank of Commerce—Richardson, J. A.
- Huron & Erie Mortgage Corp.  
The Toronto-Dominion Bank—Jeffery, J.  
Canadian Imperial Bank of Commerce—Borden, H., Ross, Hon. F. M.  
The Royal Bank of Canada—Meighen, M. C. G.
- Industrial Acceptance Corp.  
The Toronto-Dominion Bank—Lapointe, L. A.  
Canadian Imperial Bank of Commerce—Foster, Hon. G. B.  
The Royal Bank of Canada—Covert, F. M.  
The Mercantile Bank of Canada—Mitchell, H. T.
- International Utilities Finance Corp. Ltd.  
Canadian Imperial Bank of Commerce—Graydon, A.
- Kinross Mortgage Corp.  
Canadian Imperial Bank of Commerce—Currie, W. M., Glassco, J. G.,  
Graydon, A., Thomson, H. W.
- Labrador Acceptance Corp.  
The Provincial Bank of Canada—Turmel, A.
- Laurentide Acceptance Corp.  
The Royal Bank of Canada—Thomson, P. N.
- Laurentide Financial Corp. Ltd.  
The Royal Bank of Canada—Thomson, P. N.  
Banque Canadienne Nationale—Raymond, J.
- Liverpool & Canadian Mortgage & Investment Co.  
The Mercantile Bank of Canada—Benham, H. A.
- Montreal Acceptance Corp.  
The Provincial Bank of Canada—Benoit, B.  
Banque Canadienne Nationale—Bherer, W.
- Motor Dealers' Acceptance Co. Ltd  
The Bank of Nova Scotia—Kramer, R. A.
- Muttart Mortgage Corp.  
Canadian Imperial Bank of Commerce—Sale, R. M.
- National Loan Acceptance Co. Ltd.  
Banque Canadienne Nationale—Clermont, G. O.
- Niagara Finance Co. Ltd.  
The Toronto-Dominion Bank—Gardiner, F. G.  
The Provincial Bank of Canada—Chagnon, R.
- Northwest Mortgage Co. Ltd.  
Canadian Imperial Bank of Commerce—Peterson, T. O.

- Nova Scotia Savings, Loan & Building Society  
The Bank of Nova Scotia—McInnes, D.
- Pacific Finance Acceptance Ltd.  
The Toronto-Dominion Bank—Matthews, B.  
Canadian Imperial Bank of Commerce—Boyd, J. A., McCulloch, H. L.
- Pacific Finance Corp. of Canada Ltd.  
The Toronto-Dominion Bank—Matthews, B.  
Canadian Imperial Bank of Commerce—Boyd, J. A., McCulloch, H. L.
- Pacific Finance Credit Ltd.  
The Toronto-Dominion Bank—Matthews, B.  
Canadian Imperial Bank of Commerce—Boyd, J. A., McCulloch, H. L.
- Phénix Finance Inc.  
The Provincial Bank of Canada—Benoit, B.  
Banque Canadienne Nationale—Bherer, W.
- Prêt Ville-Marie Inc.  
The Provincial Bank of Canada—Brillant, J.
- Royal Trust Co. Mortgage Corp.  
Bank of Montreal—Arbuckle, W. A., Eadie, T. W. Pembroke, J.,  
Smith, H. G.
- RoyNat Limited  
The Royal Bank of Canada—Neapole, C. B.  
Banque Canadienne Nationale—Faribault, M., Hébert, L.
- Select Leased Properties Finance Co.  
The Bank of Nova Scotia—Harris, W. C.
- Simpsons Acceptance Co. Ltd.  
Canadian Imperial Bank of Commerce—Burton, E. G.  
The Royal Bank of Canada—Burton, G. A.
- Simpsons-Sears Acceptance Co. Ltd.  
The Royal Bank of Canada—Burton, G. A.
- Sterling Finance Corp.  
The Provincial Bank of Canada—Benoit, B.  
Banque Canadienne Nationale—Bherer, W.
- Traders Finance Corp. Ltd.  
Bank of Montreal—Sheppard, G. H.  
The Bank of Nova Scotia—Jackman, H. R.  
The Mercantile Bank of Canada—Palmer, K. B.
- Western Savings & Loan Association  
Canadian Imperial Bank of Commerce—Peterson, T. O.



## APPENDIX "M"

November 7, 1966

Cash Ratio Management—  
Proposed "Twice Monthly" Averaging Technique  
(By the Canadian Bankers' Association)

The banks have been carefully considering the change in the cash ratio averaging technique embodied in Sec. 72 of the new Bill to revise the Bank Act, whereby banks would be required to "average out" twice monthly instead of monthly as at present.

The banks assume that the new technique proposed is intended to bring about quicker and more precise responses, on their part, to day to day changes in their cash position.

The banks are not at all confident that the change would, in fact, bring about these results. Indeed, on an assessment of the probable consequences in the light of the practicalities of day to day cash management, there are solid grounds for the belief that the new technique would impair rather than improve the ability of the banks to respond to changes in their cash, and would introduce unnecessary stresses on, and dislocation in, the processes of monetary control.

It is inherent in the averaging technique that a bank's response to a change in its cash position at a single point of time must be influenced by the position of its average ratio up to that time, the position of its ratio *at* that time, and by a guess as to "what is going to happen to our clearing" tomorrow, or the day after, or next week.

In making an assessment of its appropriate reaction, a bank must appraise the significance of known factors which will shortly affect its clearing position. For example, a bank may know it is going to lose a large term deposit maturity "tomorrow". It may know of a large securities delivery or a large money market transaction, or a large loan pay-down, or conversely a large draw-down under a loan authorization. If a bank's action is largely in response to an appraisal of known factors, it may *appear* from the standpoint of Bank of Canada to be unnecessarily "potting up" cash or vice versa, when what it is actually doing is forestalling a larger adjustment later.

More often than not, however, a bank must react to changes in its cash on the basis of an appraisal of uncertainties. These uncertainties include the effect of action initiated outside the bank itself, not only by customers of other banks but also by Bank of Canada and government. Each bank in the system is thus preparing for uncertainty and it would, of course, be unrealistic to expect that the sum of these preparations by individual banks would neatly, and smoothly "cancel out". It is inherent in the averaging process that every bank will on occasion make a bad guess which will result in such bank, carrying, the next day, a higher or lower cash ratio than turned out to be necessary—after the event.

The foregoing outlines practical considerations in respect of a bank's response to changes in its cash ratio. But in addition there is also the question whether the money market mechanism at the banks' disposal is adequate to permit an effective response after the decision as to the amount and direction of the response has been made by the bank concerned.

There is no doubt that the money market has increased in scope and sophistication in recent years. Paradoxically, however, the nature of the development of the market has tended, in a number of important respects, to limit its effectiveness as a means of rapid and precise adjustment of bank cash.

The proliferation of money market paper *outside* the ambit of day-to-day loan collateral has tended to reduce the demand for day-to-day loans in relation to the potential supply of bank funds for that market. This situation has been aggravated by the tendency for money market dealers to finance securities which are day-to-day loan collateral through "buy-back" deals to provide a deposit facility for customers, or to obtain finance in other ways through the "country banks".

In turn, the avenues of financing presented by the country banks make it less certain that the calling of a day-to-day loan will result in a clearing gain to the calling bank. To the extent that dealers are able to respond to a call by borrowing from a "country bank" which carries its account at the calling bank, the effect of the transaction, from the standpoint of the calling bank, is vitiated.

Bankers' Acceptances, while an addition to day-to-day loan collateral, have also introduced a new element of difficulty in cash ratio management. A bank may be anxious to employ funds and will have reduced its rate accordingly. The response can be, and frequently is, inhibited by the fact that dealers wishing to borrow from that bank, cannot do so to the extent that their available collateral comprises bankers' acceptances bearing the name of the bank concerned.

Canada treasury bills, the most conventional of money market instruments, appear to have lost ground as such, if only because dealers and their customers have a good many other short paper alternatives at their disposal. It is significant in this regard that whereas in the past five years the amount of treasury bills outstanding has increased by \$285 millions, the amount held outside the banking system and government accounts has decreased by \$170 millions, having been cut almost exactly in half, and now representing less than 8 per cent of the total outstanding.

The foregoing are technical factors which tend to limit the responsiveness of the money market to action taken by the banks. But it should be remembered that even under the most favourable conditions, the ability of the banks, as a whole, to employ money in the market depends on the willingness of dealers to borrow.

In brief, the money market through which the banks are expected to respond, quickly, to changes in their cash position, is not by any means an "automatic" smoothly operating mechanism. Indeed, there are times when a bank, endeavouring to transmit its liquidity to the market, finds itself "pushing on a piece of string".

In summary to this point: The nature of the response of any bank to changes in its cash position must inherently be "imprecise" because of the element of guesswork involved in the averaging technique and because of manifest imperfections of the money market.

These considerations notwithstanding, it does appear obvious that looking at the system as a whole, the results in terms of average cash ratio for all banks combined, and on the basis of a one month averaging period, do exhibit a quite remarkable degree of precision. Indeed, it is difficult to visualize the system working more closely to the required minimum monthly average unless each

bank were simultaneously blessed with perfect foresight and also had a perfect money market mechanism with which to work.

We would emphasize at this point that in our view this satisfactory result over-all is in large measure the consequence of the monthly averaging period itself.

Over the course of a month, inevitable bad guesses and inevitably unforeseen large swings in either direction have a fair chance of "averaging out". Moreover, in the course of a month there is a certain self-compensating rhythm in large periodic monthly payments, which rhythm tends to cushion their impact on the position of individual banks. Monthly payments involving the private sector and government are a major element in this category.

From this, in the opinion of the banks, the following important conclusions must emerge.

A change to a fortnightly averaging period would do nothing to eliminate or reduce the element of uncertainty inherent in any averaging technique.

Nor would the change do anything to improve the money market mechanism through which the banks must operate.

But the halving of the averaging period would mean that self-compensating factors would have less time to work out. The "uncertainty factor" would, in effect, be doubled.

Thus, rather than leading to "quicker reactions" on the part of individual banks, halving of the averaging period would, in our considered opinion, tend to dull or to delay responses.

For example, the reaction of a bank to a sizeable clearing loss or to the anticipation of a sizeable clearing loss would in all likelihood be to carry more cash than would be the case if there were more days left in the averaging period for known or anticipated offsetting influences to even out the position. It seems fundamental that the increase in the risk factor would inevitably lead to a higher degree of caution in approach to day-to-day changes in the cash, and, over-all, to an increased "liquidity preference" in terms of a wider positive spread between the actual average cash ratio and the required average cash ratio.

This consideration would be especially germane to the position of a small bank (and there may well be more of them in the next ten years) where clearing swings would be disproportionately large in relation to the cash base.

The introduction of a statutory variable secondary reserve requirement will, we think, on balance be a further influence tending, certainly at times, to dull the response of the banks to variations in cash. Anticipation of an increase in the secondary requirement will introduce a new, and on occasion a major, element of uncertainty. In the context of a fortnightly averaging period this may reasonably be expected to slow down day to day response to variations in cash.

Much the same may be said about the banks' response to their own interpretation of official monetary policy generally. The shorter the averaging period the greater the impact of misinterpretation and the greater the incentive to "wait and see" before committing surplus cash, to the detriment of the position of another bank or banks in a short cash position.

Finally, and in the context of the role of the money market, attention has already been drawn to the imperfections of that market in point of a mechanism



for ready adjustment. A bank, under the new procedure, may be faced with a large clearing loss on, say, the second last day of the first averaging period within the month. It has good reason to believe that the situation would adjust itself on, say, the first day of the second averaging period. Under the present procedure the reaction would be to "leave it alone it will cure itself". Under the proposed procedure the more likely result could be the unnecessary transmission of pressure to the money market.

In brief, after an attempt carefully to think through the practical implications of the new procedure, the banks are forced to conclude that the results flowing therefrom are much more likely to conduce to slower, and less precise, reactions to changes in cash than to bring about the reverse situation which is apparently desired.

In the opinion of the banks, a more constructive approach to the problem of quicker reactions, if indeed there is one, would be to improve the facilities for adjustment by the banks, within the framework of the existing monthly averaging technique.

In this context a major factor tending to a cautious approach on the part of the banks is the fact that access to the Bank of Canada by way of "advances" is discouraged, first by the requirement that advances must be taken (or at least paid for) on the basis of a full seven days' accommodation, and secondly, by the penalty which attaches to a second advance in any one month. We think it obvious that both these procedures would need re-thinking in the context of a twice monthly averaging period. But, bearing in mind that the shorter averaging period would automatically increase the uncertainty factor, the result would in all probability be no net gain in point of facility and speed of response.

On the other hand, a revised policy in respect of access to the Bank of Canada (which should also include an upward revision of the banks' credit lines with Bank of Canada), combined with retention of the monthly averaging period, would in our opinion lead to quicker responses on the part of individual banks, and might generally conduce to a narrower margin between required and actual average ratios for the system as a whole.

Uncertainty is "in the contract" in point of cash ratio management. The facilities for adjustment are in any event far from perfect. A shortening of the averaging period will in our view do nothing to reduce the impact of uncertainty but will rather compound it, nor will it relieve the pressures on the money market, but will rather tend to subject it to greater and unnecessary elements of strain.

**APPENDIX "N"****PROPOSAL FOR DEPOSIT INSURANCE**  
(By the Canadian Bankers Association)

This memorandum relates to the indication given by the Minister of Finance in introducing Bill C-222 that the Government will inaugurate in the near future a system of deposit insurance in Canada. Though major details of the proposed system may still be under study, the general outline set out by the Minister was sufficiently clear, and the implications are sufficiently important, as to warrant making certain preliminary observations at this time. These observations deal only with the main issues involved, and in putting them forward at this time the banks would reserve the right to comment in greater detail should legislation in fact be introduced.

The banks believe that what needs to be kept most clearly in mind in this matter is that no system of insurance in itself can provide the desired guarantee of the safety of public deposits in financial institutions. The most effective guarantee can only come about as the combined result of sound management within the institutions themselves backed up by an adequate system of governmental supervision and inspection, and beyond that by the capacity of both national and international public authorities to avoid catastrophic economic declines. In Canada the lessons of experience led to the relatively early development of a sound management and supervisory pattern in our banking system, with the result that for more than forty years there has never been any serious concern about the safety of bank deposits. Events of the past few years, however, have raised increasing questions with respect to the position of public deposits in institutions that do not come under a proven system of supervision and inspection.

Belief that this problem might be met by establishing a system of deposit insurance was undoubtedly influenced by the insurance system in effect in the United States. There is, however, no real parallel between the situation in Canada today and the situation in the United States either in the early 'thirties when the U.S. system was introduced or in the present day.

At the beginning of 1933 there were nearly 17,800 commercial banks in operation in the United States, not to mention the large number of nonbank savings institutions as well. At the end of the nation-wide "banking holiday" in March of that year, which closed all commercial banks, fewer than 12,000 were licensed to reopen for business. Some 3,000 of the balance were eventually reopened, but over 2,000 were liquidated or consolidated with other banks. In short, the U.S. system of deposit insurance was established in conditions of extreme crisis in the banking and financial system as a whole. There can be no doubt that in this situation the new system helped both to restore a much-battered public confidence in the U.S. banking system, to provide a longer-run answer to the problems of excessive bank failures and of destructive "runs" on banks that had afflicted the decentralized unit-banking system of the United States for most of its previous history, and to bring about greater uniformity among members of the Federal Reserve System and non-member banks. Close study of the U.S. experience will reveal, however, that the crucial element in

the operation of the insurance system over the past three decades has been the effective enforcement of standard supervision and inspection over the thousands of deposit-taking institutions of all sizes and types that operate in that country.

In the present Canadian situation, of course, there is no question at all as to the fundamental adequacy of the supervisory arrangements established under the federal banking or trust and loan company legislation. The real problem has to do with some of the institutions that are provincially incorporated and whether their standards of operation are to be brought up to those required under federal legislation.

One of the most disturbing aspects of the proposals that have been made lies in the suggestion that the system of deposit insurance and its associated supervisory standards is to be made obligatory for the banks and other federally incorporated institutions where in fact the system of supervision has proven entirely satisfactory, while in the realm of provincially incorporated institutions where higher supervisory standards are needed the system would apply only "where this was desired by the institution and the provincial government concerned". If one could be sure that the scheme proposed would in fact bring about the desired improvement in supervision of provincially incorporated institutions, it would merit consideration even though there would be no advantage to the public with respect to the federal institutions and though there would still be questions regarding the sharing of costs in the form of insurance premiums. If there can be no assurance on the question of adequate supervision, however, the whole exercise loses its point.

On the matter of premiums, it is well to be clear as to what would be involved. Costs of the insurance system would depend, first, on the amount of additional inspection services required, and second, on the size of guarantee fund it was felt desirable to build up. The Government in turn might provide some or all of the money required for this fund. But whatever the resulting net costs left to be met by the participating institutions, the sharing of these costs should surely have some relationship to the requirements for additional protection of the public interest in the various kinds of institutions involved.

To sum up, it cannot be emphasized too much that the real objective at issue here is the extension of better supervision and inspection to that segment of Canadian deposit-taking institutions that is not now adequately supervised. The Minister has indicated that federal-provincial consultation would be necessary in working out arrangements for the insurance scheme. Would it not be preferable in such consultation to try first to work out with the provincial authorities an effective system of inspection, since it is the soundness of an institution rather than the insurance arrangements themselves which is the real objective to be attained?

Toronto, October 18, 1966





OFFICIAL REPORT OF MINUTES  
OF  
PROCEEDINGS AND EVIDENCE

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LÉON-J. RAYMOND,  
*The Clerk of the House.*

HOUSE OF COMMONS  
First Session—Twenty-seventh Parliament  
1966

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STANDING COMMITTEE  
ON

FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. HERB GRAY

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MINUTES OF PROCEEDINGS AND EVIDENCE  
No. 23

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THURSDAY, NOVEMBER 10, 1966

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Respecting

Bill C-190, An Act to amend the Bank of Canada Act.

Bill C-222, An Act respecting Banks and Banking.

Bill C-223, An Act respecting Savings Banks in the Province of Quebec.

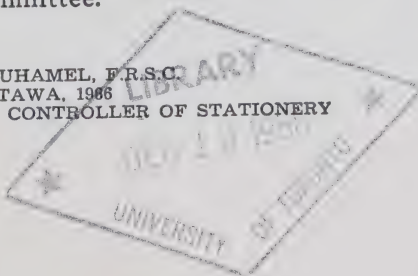
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WITNESSES:

*From the Canadian Bankers' Association:* Messrs S. T. Paton, President; Leo Lavoie, Vice-President; J. H. Coleman, Vice-President; R. M. MacIntosh, Joint General Manager, Bank of Nova Scotia; J. R. Sharwood, Deputy General Manager, Canadian Imperial Bank of Commerce.  
*Also:* C. F. Elderkin, Inspector General of Banks and Denis Baribeau, Research Assistant to the Committee.

ROGER DUHAMEL, F.R.S.C.  
OTTAWA, 1966

QUEEN'S PRINTER AND CONTROLLER OF STATIONERY





STANDING COMMITTEE  
ON  
FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. Herb Gray

*Vice-Chairman:* Mr. Ovide Laflamme

and Messrs.

Addison,	Comtois,	Lind,
Basford,	Flemming,	McLean ( <i>Charlotte</i> ),
Cameron ( <i>Nanaimo-</i>	Fulton,	Monteith,
<i>Cowichan-The Islands</i> ),	Gilbert,	More ( <i>Regina City</i> ),
	Irvine,	
Cashin,	Johnston*,	Munro,
Chrétien,	Lambert,	Valade,
Clermont,	Lamontagne,	Wahn—(25).
Coates,	Langlois ( <i>Mégantic</i> ),	

Dorothy F. Ballantine,  
*Clerk of the Committee,*

---

\*Replaced Mr. Leboe at the afternoon sitting, November 10, 1966.

ORDER OF REFERENCE

THURSDAY, November 10, 1966.

*Ordered*,—That the name of Mr. Johnston be substituted for that of Mr. Leboe on the Standing Committee on Finance, Trade and Economic Affairs.

Attest.

LÉON-J. RAYMOND,  
*The Clerk of the House of Commons.*





## MINUTES OF PROCEEDINGS

THURSDAY, November 10, 1966.  
(41)

The Standing Committee on Finance, Trade and Economic Affairs met at 11.05 a.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Addison, Chrétien, Clermont, Comtois, Flemming Gilbert, Gray, Laflamme, Lambert, Langlois (*Mégantic*), Lind, Monteith, More (Regina City) Wahn—(14).

*Also present:* Messrs. Caouette, Grégoire, Johnston, Laprise, and Latulippe.

*In attendance:* Messrs. S. T. Paton, President. The Canadian Bankers' Association and Vice-President and Chief General Manager, The Toronto Dominion Bank; Leo Lavoie, Vice-President, The Canadian Bankers' Association and Vice-President and General Manager, La Banque Provinciale du Canada; J. H. Coleman, Vice-President, The Canadian Bankers' Association and Chief General Manager, The Royal Bank of Canada; W. T. G. Hackett, General Manager (Investments), Bank of Montreal and Chairman of Canadian Bankers' Association Bank Act Revision Committee; Gilles Mercure, Assistant General Manager, La Banque Provinciale du Canada; F. L. Rogers, Economic Adviser, The Bank of Nova Scotia and Chairman, Canadian Bankers' Association Economists Committee; R. M. MacIntosh, Joint General Manager, Bank of Nova Scotia; J. R. Sharwood, Deputy General Manager, Canadian Imperial Bank of Commerce; J. H. Perry, Executive Director, the Canadian Bankers' Association; C. F. Elderkin, Inspector General of Banks; Miss M. R. Prentis and Mr. Denis Baribeau, research assistants.

The Chairman presented the Sixth Report of the Sub-committee on Agenda and Procedure, dated November 9, 1966, which is as follows:

Your Sub-Committee on Agenda and Procedure met at 3.45 p.m. this day and has agreed to recommend as follows:

- (a) That the Committee meet at 11.00 a.m. and 3.45 p.m. on Thursday, November 10th, and that there be no evening meeting on that day;
- (b) That there be no meeting on Tuesday, November 15th;
- (c) That, in accordance with its Order of Reference of October 25, 1966, the Committee engage the services of Denis Baribeau, B.Comm., of the University of Ottawa, and that he be paid such per diem allowance as the Chairman may be able to negotiate, subject to the approval of Mr. Speaker;
- (d) That the Chairman request that Miss M. R. Prentis, B.Sc. (Econ.), of the Department of Finance, be seconded to the Committee to work with Mr. Baribeau in assisting the members of the Committee.

On motion of Mr. Lambert, seconded by Mr. Addison, the report was approved.

The Chairman introduced Miss Prentis and Mr. Baribeau.

The Committee resumed consideration of the banking legislation.

Mr. Elderkin, in answer to a question raised at an earlier meeting, tabled the following exhibits:

*Exhibit No. 18: Classification of Loans in Canadian Currency of the Chartered Banks of Canada as at September 30, 1966.*

*Exhibit No. 19: Classification of Deposit Liabilities Payable to the Public in Canada in Canadian Currency of the Chartered Banks of Canada as at September 30, 1966.*

On motion of Mr. Clermont, seconded by Mr. Comtois,

*Resolved*,—That Exhibits No. 18 and No. 19 tabled by the Inspector General of Banks be attached as appendices to this day's Minutes of Proceedings and Evidence. (*See Appendix "O"*).

Messrs. Paton, Coleman and MacIntosh were questioned.

At 12.55 p.m. the Committee adjourned until 3.45 p.m. this day.

#### AFTERNOON SITTING

(42)

The Committee resumed at 3.50 p.m., the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Addison, Clermont, Comtois, Fulton, Gilbert, Gray, Johnston, Laflamme, Lambert, Lind, Monteith, More (*Regina City*), Wahn—(13).

*Also present:* Messrs. Asselin (*Charlevoix*), Caouette, Grégoire and Latulippe.

*In attendance:* The same as at the morning sitting and Mr. J. R. Sharwood, Deputy General Manager, Canadian Imperial Bank of Commerce.

Questioning of the witnesses was resumed and Messrs. Paton, MacIntosh, Lavoie, Coleman, Baribeau and Sharwood answered questions directed to them by the members.

In answer to a question, Mr. Paton tabled a paper entitled *Some Brief Comments on the Profitability of the Canadian Banking Industry*, which on motion of Mr. Lambert, seconded by Mr. More (*Regina City*) is attached as an appendix to these Minutes of Proceedings and Evidence. (*See Appendix "P"*).

In reply to a question, Mr. Paton referred to a paper entitled *Table of Costs for a Personal Instalment Loan or Advance in the Principal Amount of \$1,000 repayable in Approximately Equal Monthly Instalments as Indicated*. Copies

were not immediately available, but he agreed to provide them to the Clerk who was instructed to distribute them to the members.

At 6:05 p.m. the Committee adjourned until Thursday, November 17, 1966, at 11:00 a.m.

Dorothy F. Ballantine,  
*Clerk of the Committee.*





## EVIDENCE

*(Recorded by Electronic Apparatus)*

THURSDAY, November 10, 1966.

The CHAIRMAN: Gentlemen, I now call the meeting to order. First, I should bring to your attention the report of the subcommittee on agenda and procedure which met at 2.35 p.m. Wednesday, November 9, and agreed to recommend as follows:

(See MINUTES OF PROCEEDINGS)

As you know, the Committee felt it would be useful if it had its own staff to assist with matters of reference and research. In line with this recommendation and in the authority given to the Committee by the house, I made certain inquiries and recommended to the steering committee the individuals whose names are presented to you. I might elaborate a bit on the two individuals in question.

Miss Prentis did her undergraduate work at the London School of Economics; her graduate work at Oxford and Columbia and has had experience both with one of the chartered banks, a firm of consulting economists and the staff of the Porter Commission, and is now with the economic analysis division of the Department of Finance. She is with us now and I would ask her to stand and take a little bow.

Professor Baribeau has his Bachelor of Commerce degree from the University of Ottawa which also awarded him a Master of Arts in economics. He was with the Department of Finance, also in the economic analysis division for several years and he is presently lecturing in money and banking in the true Canadian fashion in that he gives one course in monetary theory in French and another course in money and banking in English. I think he would be well suited to provide practical assistance for us. I should explain, because of the requirements to give lectures and so on, Professor Baribeau would not be able to be with us for our morning sessions and in general, because of the possibility of work and because the steering committee and myself thought it useful not only to borrow someone from the official sector but also from the university sector so that we should have a team of two individuals, we are recommending to the Committee that the arrangement I have outlined, the engagement of Mr. Baribeau and the seconding of Miss Prentis, be adopted by the Committee as the most practical method. Professor Baribeau, I think, has just come in. He probably had some difficulty in finding parking space. If you would like to come and sit down here, Professor Baribeau. I know you have to go and give your first lecture at 11.30. We just thought it would be nice if the Committee could see who you are. If there is no discussion on the report I have given so far—perhaps I should invite it—would someone move the adoption of the report?

Mr. LAMBERT: I so move.

Mr. ADDISON: I second the motion.

Motion agreed to.

The CHAIRMAN: I should outline, naturally, the use of staffs by committees is something of an experimental matter and an evolutionary process, along with the development of our committee structure itself, so to some extent we will have to develop the procedure as we go along. The steering committee, I think, in discussing the matter yesterday did agree with the suggestion I am going to make now. First, that a request for the assistance of our research staff be channelled through myself as Chairman and in my absence the Vice Chairman, Mr. Laflamme so that it can be kept on an orderly basis. This, of course, provides no problem during our sessions when one member or another may say: Mr. Chairman, could we have this particular point looked into further and so on. I think this is the most orderly way to do it.

We will have one or both of our research assistants in attendance at all of our meetings. We will work out an appropriate schedule so that there will be no conflict with Mr. Baribeau's responsibilities, and so on. I will at this time formally request—I am sure there will be no problem—the full co-operation with them on the part of the Department of Finance and other relevant government departments and the Canadian Banking Association and other witnesses that may be before us. The steering committee also, I think, suggested that in effect the assistance as such is for the Committee in particular.

Before we get back to our questioning of witnesses, I think, Mr. Elderkin, you have some material to table in answer to questions that were raised. Would you describe it for us?

Mr. C. F. ELDERKIN (*Inspector General of Banks*): Mr. Chairman, at the request of the Committee I am tabling Exhibit no. 18, Classification of Loans in Canadian Currency of the Chartered Banks of Canada as at September 30, 1966, and Exhibit No. 19, Classification of Deposit Liabilities payable to the public in Canada in Canadian currency of the Chartered Banks of Canada as at September 30, 1966.

The CHAIRMAN: May I have a formal motion to append them to our minutes?

Mr. CLERMONT: I so move.

Mr. COMTOIS: I second the motion.

Motion agreed to.

The CHAIRMAN: Now, there is one other suggestion I am going to put forward as to procedure which I was asked to do by the steering committee. It is that we should complete this first round of general questioning, as we are going to do, and then, starting with our second round, we permit a more orderly study dealing section by section with this brief. In other words, that we complete our questioning on each section as they are presented in the brief, and then once we do that we will proceed to questioning on any matters which are of interest to the Committee which are not dealt with specifically in a related fashion by the sections of the brief.

(Translation)

Mr. GRÉGOIRE: Mr. Chairman, I would object to this manner of proceeding, because at the present time we are studying the brief of the Canadian Bankers'



Association, we are not only studying that, but we are studying Bill C-222 and if there is something to be studied clause by clause. It is not therefore the brief from the Bankers' Association, but Bill C-222. So, I can't see what advantage there is in studying this brief, paragraph by paragraph, all we have to do is study Bill C-222 clause by clause. But I think, Mr. Chairman, that what I say is quite logical.

Mr. COMTOIS: Should discussion at this stage not be limited to Committee members?

An hon. Member: No. At this time, the discussion—

Mr. GRÉGOIRE: I have not entirely made my point, Mr. Chairman. A Member has the right to come and sit in this Committee and say what he wants but he has no right to move or vote on motions. I refer to the Rules governing our procedure. I have not seen any other rule to any other effect.

The CHAIRMAN: I think I should complete your interpretation of the Rules, because the Committee has the right to set limits as to number, content and form of questions which are asked by Members who are not officially members of the Committee.

Mr. GRÉGOIRE: You are imposing closure, are you?

The CHAIRMAN: No, I am not, you are using the word, what I am referring to are the Rules governing our procedure.

Mr. GRÉGOIRE: It is not in the Rules?

Mr. COMTOIS: Meanwhile, while we await enlightenment could Mr. Elderkin tell us more regarding second mortgages of chartered banks?

(English)

Mr. ELDERKIN: What type of information did you wish?

Mr. COMTOIS: You were supposed to look to see if the chartered banks were allowed to go into second mortgages.

Mr. ELDERKIN: Mr. Chairman, the power to lend on second mortgages is in clause 75(1), where they may lend on real or immovable property. The section to which we referred the other day, namely, subsection (3) is a limiting clause governing the extent they can lend, which combines the amount they may lend on any property either by first or second mortgage to a total of 75 per cent of the value of the property. Mr. Fulton raised a question about laws in certain provinces. I believe this applies in British Columbia and in Ontario as well.

The CHAIRMAN: Excuse me, I think it would be more orderly if we deal with this point of procedure and then proceed to complete any unanswered questions from the preceding day that have been held over for that specific purpose. I do not say we have to arrive at a formal decision on this precise point at this time but I draw to the attention of the Committee and others participating in its work the following subparagraph 5 on page 62 of the reprint of the rules:

Any member of the House of Commons who is not a member of a standing committee may, unless the house or the standing committee otherwise orders, take part in the deliberations of the standing committee, but shall not vote or move any motion or any amendment or be counted in the quorum.

I mention that only to complete, as I was saying before, the interpretation of this clause by Mr. Grégoire.

*(Translation)*

As far as I am concerned, as Chairman, it is my intention to treat every member on the same footing, any member who wishes to take part in the work of the Committee, but at the same time I feel I must give some priority to the actual members of the Committee who have the responsibility of taking decisions and so, I interpret this clause of the Rules, and if necessary, I will ask the Committee for a formal motion limiting the work and the various forms of interventions of Members who are not members of the Committee.

*(English)*

I would like to try and avoid that if possible and let the Committee rely on my attempt to be fair and reasonable in dealing with this question. It may be that those members who are present who are not members of the Committee may prefer that to a formal motion which may be more restrictive than the intentions of the Chairman at this point. I leave this to the judgment of those concerned.

*(Translation)*

MR. GRÉGOIRE: Mr. Chairman, may I continue on this?

*(English)*

The CHAIRMAN: No, I also feel that if someone who is not a member of the Committee is not to vote or move any motion or any amendment or be counted in the quorum, it follows that someone who is not a formal member of the Committee cannot raise a point of order because a point of order is, in a sense, a form of proposal. Therefore, while I will not hesitate to receive brief suggestions from any person attending these meetings as a member, whether a formal member or not, with respect to procedure, because after all the suggestions are often useful whether they come from a formal member of the committee or not, I do not think it would be appropriate in the light of the references in the rules to votes or moving motions, amendments, and so on, to permit those who are not actual members of the Committee to become involved in formal points of order; although, I certainly will not hesitate to accept suggestions on the order and procedure to the Committee from those who are not members, within reasonable limits. With respect to the point that has been raised about our order of business, I want to make clear that I intend to permit this round of questions in which we are now engaged to be completed and that this round would not be limited in any way as to the subject matter. Mr. Lind is asking questions. There are some here who are members of the Committee who have not asked questions. There are some members here who are not members of the Committee—I see Mr. Caouette and so on who, I think would like to ask some questions and they will have the right to do so. But, it was the view of the steering committee, and Mr. Monteith will agree with me, although we felt we should not be so tight, shall I say, as to have a specific motion but would permit a more orderly discussion of the topics that the witnesses may want to bring to our attention, that we proceed with the topics in the order presented in the brief on the understanding that in discussing these topics, closely related matters could be brought up, whether they specifically refer to the brief or not. And that once we went through the topics in the

brief, or the supplementary brief, as in the case of the Canadian Bankers Association, there will be full opportunity for any member and after that for others to raise any subjects related to the bills discussed which they feel these witnesses or others could deal with. This proposal was put forward by people on the steering committee and it seemed to receive the favour of all those present and I think, just about all the parties on the Committee. This was done from the point of view of permitting a more focused discussion, if I may use that phrase, with respect to specific briefs. If, perhaps, I did not explain what I had in mind as well as I might have at the beginning, I think that on reflection you may feel this is a useful procedure to try.

As I said previously, and I think Mr. Monteith and others will agree with me, if this suggestion does not seem practical for one reason or another, perhaps because of the form of the brief or other reasons, obviously we are going to try and be flexible. I just mention this now so we will not get into this discussion once we actually begin our questioning. I want to stress that as far as this round of questioning is concerned it is my intention as Chairman to go on in the same format as we have been using up to now.

Mr. MONTEITH: Mr. Chairman, may I just say one word. I think it was felt that in perusing the evidence subsequently, it would be better if we completed the first round, as you are suggesting, and then questioned on one topic until we had more or less exhausted it. True, as you say, there is no harm in mentioning a similar topic later but the evidence, then, would have everything to do with interest rates in the one section. You would not have to be thumbing all over the evidence to try and find the relevant parts.

The CHAIRMAN: That is right and I think you agree—I want to repeat this—that if there are matters not treated in these briefs which people want to raise as we go through the topics which seem to be of most interest to the witnesses and related topics which obviously arise, then, of course, members will be able to ask questions on any relevant matter, the test of relevancy being the subject matter of the legislation referred to us. In other words, the aim here is to permit a more focused and orderly discussion without any limit.

*(Translation)*

Mr. LAFLAMME: Mr. Chairman, may I say a word. Just to clarify the debate and to examine every matter thoroughly and in a more orderly fashion, this has been our sole intention regarding the agenda.

Mr. GRÉGOIRE: I must conclude that any point of order which is raised by a member who is not an official member of the Committee, is mostly rejected because he has no right to bring a motion or to second the motion, nor to vote, and does not count in a quorum. That means that he has no right to vote on any point of order?

The CHAIRMAN: I feel that this is the case, because a point of order is a form of motion but I would like to reserve this opinion and study it more thoroughly. But at the same time, those who are not official members of the Committee should try, as far as possible, to limit their participation so far as points of order are concerned or matters relating to the agenda, because it must be recognized that other official members of the Committee do have the responsibility to take decisions and to advance the work of the Committee and to make an official



report to the House of Commons. This is what I mean when I speak of using the Committee as efficiently as possible.

Mr. GRÉGOIRE: Perhaps when you study that you will also examine the problem of questions of privilege which is also a point of order. I would ask you if a member, who is not officially a member of the Committee, can raise a question of privilege. Does this mean that if your privileges are not accepted you cannot raise them?

The CHAIRMAN: No, Mr. Grégoire, if you want to pursue this interesting matter I think I could give you at once a reply that you will not like, if you wish to go on with this. Because speaking as a lawyer, I might say that I am used to giving considered answers to judges who put questions like yours. I think it is quite possible that a question of privilege is a point of order and will be treated on the same footing, but I think it would be better to continue with our line of questioning and with the work of the Committee.

*(English)*

Therefore, gentlemen, I think I will ask Mr. Elderkin to complete his presentation of information which he was giving in answer to points that have been held over until today for that purpose.

Mr. ELDERKIN: I may be repeating myself but the power to lend on real and immovable property is in clause 75(1)(c), on real and immovable, as well as personal property. The clause, 75(3), is a limiting clause. It limits the amount which may be loaned on real or immovable property. Now in certain provinces, British Columbia, as Mr. Fulton raised the point, and I understand in Ontario, too, the title actually passes to the lender under a mortgage. Therefore, there is not real or immovable properties that are loaned on as a second mortgage. What the loan becomes is a mortgage on equity of redemption but it is really the same thing under a different name.

The CHAIRMAN: Also, I think that, Mr. Paton, your group has some material to present in answer to questions that were held over to this morning. I think this would be a useful way to proceed to get this material out of the way. I was mistaken. There is no additional answer the association wants to give.

Mr. MONTEITH: Mr. Chairman, may I just bring up one point. In my questioning last Tuesday, I had raised the matter, just for instruction of laymen like myself, of the procedure of banks commencing business and how they go into the business from there on. That question was left in abeyance, not that I want it answered right now or anything, but at some stage I would like, purely for my own edification, some answer.

The CHAIRMAN: I think it would edify other members as well. Mr. Elderkin or Mr. Paton, do you have an answer to that now? I think this is a question that was held over and perhaps could be dealt with before we give the floor back to Mr. Lind.

Mr. PATON: I might, possibly, Mr. Chairman, try to accommodate Mr. Monteith. I am going to take it from the time when the bank is ready to open its doors which, I think, was the stage that you were particularly interested in, Mr. Monteith. Having completed the necessary legal requirements under the Bank Act, the bank in opening its doors has as a start as its assets, paid-up capital, and then its liability would be one liability only, that to the shareholders. They

would obtain the required till money, as you have indicated, from the Bank of Canada.

Mr. MONTEITH: How do they get that till money, what do they give for it?

Mr. PATON: They would have to withdraw part of their capital to pay for it. They then would have, their liability to their shareholders and their till money plus the assets represented by the shareholders' contributions. This till money would be part of their reserve with the Bank of Canada, as it is in the case of all other chartered banks.

Mr. MONTEITH: What they pay for their till money is part of their reserve with the Bank of Canada?

Mr. PATON: The actual till money in the tills is part of their reserves, as it is in all other cases. The Bank of Canada 8 per cent reserve consists of deposits with the Bank of Canada plus the Bank of Canada notes we have in all our branches for servicing our customers. So, a new bank starting would start in on that basis and then would proceed to compete for deposits and make loans in a normal manner.

Mr. MONTEITH: Are you allowed to make any loans before you take any deposits?

Mr. PATON: They would have surplus funds from their capital contributions which they could loan out. From that, of course, and prior to this, has come the cost of setting up bank premises, and so on. They would have the use of their available funds, however, to make loans.

The CHAIRMAN: Mr. Elderkin, do you want to supplement that in any way?

Mr. ELDERKIN: No, I think not, Mr. Chairman. I think that Mr. Paton has covered it very fully up to the time they actually start to take deposits from the public. They will, of course, be using the funds they receive from the issue of capital stock.

Mr. MONTEITH: When a reserve is increased over and above the till money, what form exactly does that take?

Mr. PATON: That would take the form of a deposit with the Bank of Canada. They would then immediately enter into the same arrangement as the other banks.

Mr. MONTEITH: That deposit simply reduces the assets of the bank and gives an asset to the Bank of Canada in the amount of that additional?

Mr. PATON: It reduces the availability of the assets which they can invest in loans and other investments. It is part of their investments out of their assets which would then constitute a deposit with the Bank of Canada.

Mr. MONTEITH: That is the portion that does not derive any interest, then?

Mr. PATON: That is correct, sir.

Mr. MONTEITH: Does this take the form of deposit of securities of any kind?

Mr. PATON: No, sir.

Mr. MONTEITH: You cannot do that.

Mr. PATON: You cannot do that. This is a deposit of cash in the Bank of Canada, held by the Bank of Canada to credit of the individual banks.

The CHAIRMAN: I must apologize to Mr. More and perhaps also to Mr. Lind because in reviewing this I think that Mr. More had not completed his questioning when we adjourned. If you would accept my apologies Mr. Lind, in this regard, I think I should give the floor back to Mr. More.

Mr. MORE (*Regina City*): Mr. Chairman, I will try to be brief. There are two or three things I want to touch on. I want to go back to the interim hearing on interest rates. Perhaps this is a hypothetical question that Mr. Paton cannot answer, but if he can I think it would be interesting: provided this legislation with its interim ceilings comes into effect, how long do you expect it might be before you would reach a position where the interim ceiling would be completely removed?

Mr. PATON: We referred to that, Mr. More, in our brief. We definitely feel that it might be considerably longer than was originally thought when the legislation was brought down. The trend of interest rates since the amendments to the Bank Act were introduced, has indicated that the figure of  $4\frac{1}{2}$  per cent is not as realistic as perhaps it might be. Therefore, if the ultimate decision is to have this ceiling removed in a two stage procedure, this  $4\frac{1}{2}$  rate might conceivably and reasonably be set at a higher figure of, let us say, 5 per cent. We still feel that a desirable situation, of course, is to have the full removal of the ceiling as a result of Bill C-222.

From all the indicators that we have, we feel that there may be a general maintenance of a higher level of interest rates than we have been accustomed to in the past. We itemize these reasons in this brief much better than I could interpolate them for you. But, in effect, in direct answer to your question, we think it may be considerably longer, perhaps 10 years, we do not know, before the tapering off to the triggering ceiling rate of  $4\frac{1}{2}$  per cent could conceivably take place.

Mr. MORE (*Regina City*): In other words, you do not expect to have reached a no-limit within the lifetime of this legislation if it passes in its present form.

Mr. PATON: Perhaps "expect" is a little too strong a word, but we can see where there could be a possibility of this happening. In any event, it would be longer than the two years that has been suggested once or twice as a reasonable interval in which this might occur.

Mr. MORE (*Regina City*): Thank you, Mr. Paton, I think that fully answers what I had in mind. Now I want to go to the insurance that this legislation proposes.

Mr. PATON: No, it does not.

Mr. MORE (*Regina City*): I beg your pardon. But there is a proposal inherent that will come up on deposit insurance. This is part of the representation—

The CHAIRMAN: I would like to make it clear at this point so that there will be no doubt about this; I consider that it is within the ambit of our responsibilities to be able to ask questions and to consider this general aspect. I think I have already reported to the Committee that it is my hope that a very detailed resolution if not the bill itself will be before the house in the not too distant future. Therefore, we must look into this in a more detailed fashion.

Mr. MORE (*Regina City*): The Minister gave this indication in an answer to a question yesterday.



The CHAIRMAN: That is right.

Mr. MORE (*Regina City*): I take it that one of the basic problems the bank faces with a ceiling limit on interest rates is in the competitive sphere. Anything, then, that increases the cost of their operation is going to affect their ability to fully compete with other near banks. This proposal, therefore, for deposit insurance, which I understand will be mandatory on the chartered banks, is going to increase your cost of doing business and competing; whereas it is not mandatory on the near banks. I take it that there are two objections from your association and the chartered banks in regard to this proposal: One, that it is not necessary in connection with your operations from the point of view of history and experience; two, it is discriminatory against you in that the umbrella does not cover all the operators. I have been doing a bit of banking for a considerable number of years and I do not think I could agree with the statement you made on compensating balances having been effective for many many years. Certainly some of us who did business with the banks were made aware of these situations, but in the last year and a half or two years it seems to be universal as far as I can learn from accounts that seek bank services. In the past if they did apply, it seems to me it was on the basis of the feeling of the bank that a larger risk was involved and this would help them in countering the risk for the money loaned. But now it seems to me it is to make up expense charges and costs of the bank more than having anything to do with risk. It has become a general operation of the bank in this regard. Is this a plausible assumption in this regard?

Mr. PATON: With your permission, Mr. More, I would like to defer to my colleague Mr. Coleman who would be very pleased to discuss this subject with you.

Mr. J. H. COLEMAN (*Vice-President, The Canadian Bankers' Association*): Mr. More, would you like my views on the deposit insurance first? There were two parts to your comments—

Mr. MORE (*Regina City*): Yes, I think this would apply because I am joining it with the question on deposit insurance.

Mr. COLEMAN: I would say that I think it is generally agreed by the banks that deposit insurance is not necessary as far as the chartered banks are concerned. We think this would be generally agreed. It is true that if it is a federal act, as it will be, that there are jurisdictional problems and presumably it might be difficult for provincial and non-bank financial institutions to get under the umbrella of deposit insurance. I think it is true that some of them will wish to do so, if for no other reason than to gain respectability. However, if it develops that this deposit insurance act embraces only the banks and a few federally incorporated trust companies, then it seems to me that it is a massive effort and a very expensive one to cover the largest area of depositors—that is, those who have accounts at the banks—and if it ends up that we were the only ones who need the protection of perhaps four out of five institutions, we find it difficult to see the justification for it from any standpoint. Does that answer your question?

To get back to the matter of compensating balances: you said it seems that it was only recently that compensating balances were required. I do not think this is strictly true, with all due respect, Mr. More. I do think that the practice has

become much more prevalent and I admit that freely. The way banks operate is that there are two ways to recover costs of operating an account. One is to get balances that will compensate them for the operation of the account, and the other is to get service charges. I think in the past it has been true that the more common way was service charges, but I think now, with the shortage of cash, that the banks prefer compensating balances. I do say categorically that, as far as our bank is concerned, we have been stipulating for one or the other in accounts that needed it from a cost standpoint as far back as I can remember.

Mr. MORE (*Regina City*): Was it cost or risk?

Mr. COLEMAN: I would say it was entirely the cost of operating the account.

Mr. MORE (*Regina City*): I accept your explanation as the word of an honourable member, in parliamentary terms.

Mr. COLEMAN: There is one point. I think this subject of compensating balances was flogged to some extent the other day, but I think I overlooked an important point in my testimony and that is the subject of float. As you know, most people who run current accounts and most companies have a number of cheques floating around the country and it is not uncommon for people to issue cheques and figure out how long it takes for a cheque to get to the bank. They might cash it at a garage and say: "Well, it will take about three days and as long as I have the money in there in three days, I am all right." But in large accounts this float amounts to many, many hundreds of millions of dollars. When a cheque is issued by a client and negotiated by the payee, he gets immediate credit for that cheque from a bank, but the person who has issued the cheque does not have to put up the money until the cheque reaches the bank. Therefore, there should be an adequate balance in the bank when the cheque is issued. You are borrowing money if there is not.

The CHAIRMAN: Is it a criminal offence to issue a cheque knowing you do not have the money in the bank?

Mr. COLEMAN: You are a lawyer, Mr. Chairman, I do not think it is, but I wish it were. My understanding is that if you do not have an account, that it is a criminal offence, but I think you can issue cheques pretty freely and not be taken to account for it.

The CHAIRMAN: I think Mr. Addison has a supplementary if Mr. More will yield.

Mr. MORE (*Regina City*): I will yield.

Mr. LIND: I am on the same subject, and I thought I was due to ask questions.

The CHAIRMAN: That is right. We have been allowing brief supplementaries, but if a questioner has not finished and if he yields—

Mr. LIND: It is about time.

The CHAIRMAN: I will take this into account. I certainly do not propose to have an extended discussion arise under the guise of a series of supplementaries. If that is what you are suggesting, I think you are quite right in complaining about that possibility.

Mr. ADDISON: Mr. Chairman, if Mr. More will allow I have a brief supplementary for Mr. Coleman. The idea of a federal insurance agency is to give credibility or dependability to near banking institutions. In the ordinary business of insurance, insurance is predicated upon experience, and while the chartered banks are federal institutions and will fall under the guise of this legislation, certainly there is no danger of the federal banks falling into default, therefore, I would suggest that while the premiums will be based upon experience, I do not believe there is any interest in the Minister's mind of making this a profitable operation. This is an insurance company operated by the government of Canada and therefore I cannot visualize premiums to the chartered banks, or any other institution for that matter, being of any significant amount in order to increase the cost they have borrowed.

Mr. COLEMAN: Mr. Addison, I hope what you say will prove to be the case. If we based the cost on the rates charged by the federal deposit insurance corporation in the United States, it would be a very expensive item for the chartered banks, or even if the costs were halved, it would amount to millions of dollars.

The CHAIRMAN: Mr. Gilbert, please be brief.

Mr. GILBERT: Are we to assume that the banks now consider service charges and compensating balances as synonymous, one and the same thing?

Mr. COLEMAN: No.

Mr. GILBERT: What is the difference?

Mr. COLEMAN: The difference is that if we analyse an account and our cost to operate the account is \$10, including a small margin of profit, because we are in business to make money, we could either charge you \$10 a month, or we could ask you to carry a balance which would, in effect, give us a \$10 coverage.

Mr. GILBERT: I will now pass, but I will ask him later to explain that.

Mr. LANGLOIS (*Mégantic*): I have one short supplementary to a statement concerning what Mr. Coleman mentioned on floating cheques. I agree there must be a considerable number of these and you actually stated when these cheques do come in, if the issuer has not yet deposited, you are advancing or making a loan to him until he does cover the cheque. On the other hand, I would like to ask this question. Is it not a common practice lately in the banks to have a series of notes in their hands and the minute a thing like that happens, the note is passed through and it is now a loan, but was formerly an overdraft which you do not have any more. If that cheque does come in the fellow has to pay the interest on it.

Mr. COLEMAN: I think it is true that some banks carry blank notes, but the point I tried to make was that sometimes those cheques are really in transit for a week and therefore, the person who issued the cheque has, in fact, borrowed the funds for the week. The note is not dated back to the date of issue of the cheque; it is dated the day the cheque comes in, therefore you who have issued the cheque have had use of those funds, the person to whom you made the cheque payable has had that money and credit for it from the time he cashed the cheque.

The CHAIRMAN: Mr. Langlois, I think to be fair to the other members who are waiting to have an unbroken series of questions, we should return to Mr. More and ask him if he has further questions.



Mr. MORE (*Regina City*): My time must be nearly up, but to finish up. Mr. Coleman, it is not really a fact that the issuer of a cheque has a loan from the time he issues the cheque; if he is mailing the cheque a considerable distance and he knows it is going to take two days before it is deposited by the person to whom he issued it, there is no loan involved there until it is deposited.

Mr. COLEMAN: I agree and that is what I thought I said.

Mr. MORE (*Regina City*): I think you said that from the time he issued the cheque he had the loan.

Mr. COLEMAN: If I said that, I was in error. I mean from the time the cheque was negotiated.

Mr. MORE (*Regina City*): Regardless of what the premium might be there is going to be an added cost and, as you say, if it were based on the American system it would amount to millions of dollars in your operation.

Mr. COLEMAN: That is right.

Mr. MORE (*Regina City*): Have you any estimate in round figures on your present operation?

Mr. COLEMAN: I beg your pardon.

Mr. MORE (*Regina City*): Can you estimate on your present operation how many millions for the chartered banks in Canada, if these were the rates?

Mr. COLEMAN: It would be \$6 million.

The CHAIRMAN: But we do not have the government proposal.

Mr. MORE (*Regina City*): No, but this gives the Committee some figure and some idea so that if we have the government's proposals, and they are similar to the American proposals, we know what the figure will be, and we can deduct from what is proposed what the amount will be in the operation.

The other thing I want to ask, Mr. Coleman, is this: Your merchandise is money and loans and the reason for compensating balances and charges is that you cannot make a mark-up that will cover all these things in your operation. I presume this is a fact. Where you have accounts with compensating balances do you also make a charge for handling the cheques in addition to the return you get from having the compensating balances maintained?

Mr. COLEMAN: If the compensating balances are large enough there are no other charges but if they are not, there could be both. When an account is analysed and when the charges are computed, the balance is taken into account. I think I mentioned that on a small account I think most banks allow one free cheque for every \$50 balance in a savings account where interest is paid; but on a current account where there is no interest paid, it is one free cheque for every \$100. In other words, if you had a \$1,000 average balance you could issue ten free cheques a month. If you did not have more than \$1,000 there would be in addition to the balance, a charge.

Mr. MORE (*Regina City*): It seems to me it should be the reverse.

Mr. COLEMAN: It is the reverse, I am sorry. You are right. It is one for every \$100 in savings and \$50 in current.

The CHAIRMAN: Well, Mr. More, I think if we count your time on Tuesday your time has expired.

Mr. MORE (*Regina City*): Well, I expected you to advise me, Mr. Chairman.

The CHAIRMAN: Oh, yes. I am not criticizing your activity in posing useful questions. I suggest I should recognize Mr. Lind.

Mr. MORE (*Regina City*): Fine.

Mr. LIND: Mr. Paton, I would like to go into this area of compensating balances also. Coming back to Mr. Coleman's statement a moment ago about the loan compensating balance being used to cover the cost of a cheque from the time it was issued by the issuer until it returns to the bank, have you not the privilege, Mr. Coleman, of stopping payment on that cheque if the current account is overdrawn when it arrives?

Mr. COLEMAN: Yes.

Mr. LIND: But this would cover your problem of "kiting" which is a term that is commonly used on the street.

Mr. COLEMAN: It would not cover our problem with the customer if we returned the cheque.

Mr. LIND: Which customer? The one who issued it?

Mr. COLEMAN: That is right. I think the person who cashed it would be disturbed, too.

Mr. LIND: That is common practice though, is it not?

Mr. COLEMAN: I hope it is not common practice, but it is done. I would say that the number of cheques returned is very, very small in relation to the number paid.

Mr. LIND: Most of us poor people in business have had cheques returned from time to time by the banks.

I would like then to say and to agree with Mr. More that you do not pay any interest and there is no liability on the part of the bank from the time the cheque was issued until it is honoured at your bank, so that—

Mr. COLEMAN: May I interrupt to say, until it is negotiated at the bank which cashes the cheque.

Mr. LIND: Until it gets back to the original bank through your clearing house.

Mr. COLEMAN: No, no, Mr. Lind, if a cheque is issued to someone or someone in Toronto issues a cheque to someone in Vancouver, the party in Vancouver goes into the bank and gets cash or credit for that cheque. From there on the funds are being used.

Mr. LIND: The funds are being used, Mr. Coleman, but at the same time, if when it gets back to Ottawa at the other end if there is not sufficient funds to cover it, it is charged back to the customer's account at the other end.

Mr. COLEMAN: But someone has had use of that money free in the meantime.

Mr. LIND: The money is no use to the person from whom you purchased the goods.

Mr. COLEMAN: It is until he has to return the funds that he got for the cheque.

Mr. LIND: May be; but it is doubtful. There is an area of argument there.

Mr. COLEMAN: Oh! Yes.

Mr. LIND: I go back to Mr. Paton again. I think the other day you stated that the compensating balances were to be used as a common practice in covering the cost of par privileges in certain cities and provinces, The Dominion of Canada, for instance, carries \$100 million which is left on deposit with the chartered banks to allow them to issue cheques at par for all over Canada. Is that correct?

Mr. PATON: It is correct to the extent that there is no compulsion on the government of Canada to carry \$100 million with us. But on balances that they hold with us, up to \$100 million, it is held free of interest paid by the banks and on any surplus over that \$100 million the banks pay interest at 90 per cent of the Treasury bill rate. That is the exact arrangements we have currently with the government of Canada.

Mr. LIND: But this is mainly for the privilege of cheques at par all over Canada, is it not?

Mr. PATON: It is for the costs of handling the government business. As a matter of fact I think we have some statistics here. We estimate that our cost of servicing the government per annum, chartered banks as a whole, is \$7 million.

Mr. LIND: Million or billion?

Mr. PATON: Seven million dollars, and that is the cost to the banks. On the arrangement we have with government regarding balances—I am assuming that a 100 million is kept right through the year which is indeed with very few exceptions, the fact, is that the total maximum earnings from the government business from these balances would be \$5 million in round figures. At the present time, from our latest cost statistics, we are providing the government with a service with an annual loss to us of \$2 million per annum.

Mr. LIND: Further on compensating balances, are the banks not using compensating balances to augment their income from your commercial accounts or current accounts? Veritably, you are charging 6 per cent on the current account plus a service charge for issuing the cheque, plus the compensating balance to cover any additional cost to that account. Is this not a means of circumventing the present ceiling on the Bank Act, or of interest rates?

Mr. PATON: No, sir. I think I answered in the same vein the other day. Costs of banking, costs of every service that we are providing, have been increasing. We have become more conscious of the need to identify these costs with the entire services we provide for the Canadian public. This is the sole reason why the compensating balances have taken a more important place in the charges that the bank has been making, but it is purely on a basis of compensating the banks for the services that they are providing and, in effect, making each department stand up by itself.

Mr. LIND: Have you the percentage in your banking association of the increase in the use of compensating balances over the last two years and one year and could you give a comparison?

Mr. PATON: No, sir, we have no record of that. This would be a matter for individual banks, Mr. Lind, because each bank has a different procedure in this connection. There is no uniform procedure.



The CHAIRMAN: Mr. Paton, perhaps to assist Mr. Lind, could you ask your individual members to supply this Committee with information on the increase and the uses of compensating balances in their respective institutions? Take the number of commercial accounts, the number on which compensating balances were applied, say two years ago, the number today, and give us those figures?

Mr. PATON: This would be rather a mammoth exercise, Mr. Lind, but certainly if you were to leave the question with me I will have an opportunity to discuss it with my colleagues at noon and report back to you at the afternoon session. My immediate reaction to this is that it would be well nigh impossible to provide meaningful figures because with any figures we provide we like to have a solid basis on which to support them.

Mr. LIND: Well, maybe I could ask you a question. Is this not a practice that has increased more rapidly over the last year than at any time in the banks' history?

Mr. PATON: Certainly, I would agree with your statement that it has increased rapidly over the past period, Mr. Lind. I do not know how far you go back when you refer to bank history, I would assume that possibly there is a good deal of accuracy in your statement.

Mr. LIND: How do you figure out these compensating balances? Taking a figure out of the air, is it roughly 10 per cent that you add to be kept there of the amount of the credit that is extended to the current account?

Mr. PATON: It may well be that in many cases this is the ultimate result, but this ten per cent is not the magic figure that we arrive at. Again, as Mr. Coleman pointed out, this is strictly based on operating costs of individual company accounts with the banks themselves.

Mr. LIND: Do you want me to go into a personal matter with the Toronto-Dominion bank?

Mr. PATON: Yes, if I could buy you a lunch, perhaps?

The CHAIRMAN: Well, Mr. Lind—

Mr. LIND: That is only an aside.

The CHAIRMAN: Not that I am suggesting that you are out of order. If I may say so as Chairman, this may be very useful to the Committee to have a particular case.

Mr. LIND: Do those compensating balances become a deposit?

Mr. PATON: Yes, the compensating balances are reflected in the bank deposits. They are held to the credit of the customer's account.

Mr. LIND: Can the banks loan against compensating balances?

Mr. PATON: They can loan against these deposits similarly as they can against any deposits in the normal banking procedure.

Mr. LIND: Then they can extend the limit of credit on that twelve and a half times against that compensating balance.

Mr. PATON: This is beyond their purview, Mr. Lind. If the bank of Canada did not make any move, they can lend this balance, but the Bank of Canada has control over just how far the banks can go.

Mr. LIND: How much control do they maintain over these compensating balances?

Mr. PATON: They do not single the compensating balances out in any way, shape or form, Mr. Lind, from the total deposit liabilities of the chartered banks.

Mr. LIND: Then in theory you can loan twelve and a half times against it..

Mr. PATON: I still have to say no to that. Perhaps in theory it might be possible.

Mr. LIND: But the possibility is there.

Mr. PATON: I do not think that is what Mr. Coleman said.

Mr. COLEMAN: I think I should say here that there might be a misconception in the minds of the members of the Committee about the compensating balances. These are all part of the total deposits of the bank. You do not look and say this a compensating balance, and this is your operating account. If you wanted to get the total of the increase you would simply say what were your deposits at this date, what where your deposits here. There is no way of telling. Compensating is an unfortunate word. These are adequate balances for the operation of the account. They are all part and parcel of the over-all deposits of every bank.

The CHAIRMAN: But, surely, sir, taking your banks as an example, you must know in some way or other which accounts have been instructed or requested or ordered to keep these balances and which have not.

Mr. COLEMAN: Every account has been instructed either to carry balances sufficient to compensate us for our efforts or pay operating charges.

The CHAIRMAN: Every account.

Mr. COLEMAN: Absolutely, every account.

The CHAIRMAN: Could the other banks present inform us of whether they have a similar policy? -

Mr. COLEMAN: I am speaking for our own bank.

The CHAIRMAN: Oh, yes, naturally. I understand that.

Mr. LIND: Why are the compensating balances asked then to be greater than will cover this cost that is laid down? Suppose after you get your 6 per cent, after you get your service charge on the cheques, the cost for carrying this account you figure out is for a small account \$10 per month, or \$15 per month, and then why do you ask the customer to keep a compensating balance that will recompense you at the rate of \$25 per month?

Mr. PATON: Could I just refer to a previous question and correct one of my answers, as I mentioned the other evening when I get into this theoretical area of banking, I sometimes get in too deeply. I should have said in reply to your suggestion about compensating balances and theory of expanding them that one of my more learned colleagues reminds me here that the compensating balance is not cash and cannot be used as a base for credit expansion. Could I correct the record and leave that at that, sir, and then refer to your question of a moment ago.

The service charge for compensating balances are alternate ways. It is not necessary that there has to be one or the other. It might be a combination of both, Mr. Lind, depending on the individual arrangements made by each bank with each customer.

Mr. LIND: If this new bank act was passed and the ceiling was lifted, is it the intention of the Canadian Bankers' Association to recommend to their chartered banks that they remove this compensating balance privilege?

Mr. PATON: I think I should perhaps say that the role of the association has nothing whatsoever to do with the operation of individual banks. The association has no power whatsoever to make any recommendation to individual banks as to how they should operate. This is solely a question for the management of the individual banks.

The CHAIRMAN: If you would like to rephrase your question as to what the banks themselves may do, perhaps it would be useful.

Mr. LIND: I would like to ask it this way then. Will the banks, after Bill No. C-222 goes through and the ceiling is virtually lifted off loans, do away with compensating balances? Is it their intention to do away with this and service charges, or are they going to maintain these two forms of income in addition to the extra interest?

Mr. COLEMAN: Mr. Lind, the rate of bank charges on a loan is related directly to the cost of money, and availability of money, and the availability influences the cost. I do not think any bank would attempt to recover the cost of operating an account through an interest charge. The interest charge that you or anyone else pay on a loan will be what the bank thinks you should pay for that money. I would say, and I think I can speak for all the banks, that adequate balances will have to be maintained to pay for the activity in the accounts or service charges will have to be paid. The interest rate is a separate factor altogether. I do not think any bank would attempt to cover operating charges through the medium of the interest rate on a loan.

The CHAIRMAN: You disagree with the Porter Commission then, where they seem to imply in one place which you quoted in your brief that the interest charge covers the administrative cost.

Mr. COLEMAN: Of a loan account. The loan account is completely separate from the operation of the current account, for handling of deposits and posting of cheques and all these things. The loan account is completely different, Mr. Chairman, from the operation of the account. We have two different things here. We have a liability account, a loan account and, as I say, one of the prime ingredients is the cost of money. The cost of operating a loan account is a small factor as well, but the principal ingredient is the cost of money.

Mr. LIND: May I go into another area then, Mr. Paton? I would like to go back to the brief of the Canadian Bankers' Association. I did not quite understand who pays the cost of the Canadian Banker's Association?

Mr. PATON: The cost of the Canadian Bankers' Association is paid entirely by the eight chartered banks.

Mr. LIND: The eight chartered banks. Are there bylaws ruling your association then?



Mr. PATON: Yes, there are bylaws by which the association governs. They go back I think to nearly 1900.

The CHAIRMAN: Perhaps it might be useful, Mr. Paton, if we asked you to obtain copies of the office consolidation of the Canadian Bankers' Association Act, and also those bylaws to which you were referring, to give you your first task.

Mr. LIND: Then you are going to answer my question. You are going to say something on bylaws.

Mr. PATON: Yes, Mr. Perry, our Executive Director, points out to me that the bylaws of the Canadian Bankers' Association have to be passed by Treasury Board.

The CHAIRMAN: Perhaps we would find it useful if we all had copies; that is, the members of the Committee, in response to your question.

Mr. LIND: Now this association naturally brings all banks together in a friendly manner, either over a cup of coffee or over a meal or something else. does this in any way inhibit competition between these eight chartered banks?

Mr. PATON: Mr. Lind, I would suggest perhaps you should attend one of these meetings. You might change your descriptive adjective. I invited Mr. Cameron to change places with me the other night and now I am giving you an invitation to join an association meeting. It is obvious we have nothing to hide.

The CHAIRMAN: I might inform the Committee that when I heard Mr. Paton invite Mr. Cameron to change places with him, I thought the millenium was arriving.

An hon. MEMBER: I will pass on that one.

Mr. LIND: If you will turn to your Bankers' Association brief where you outline the services you do for the government, you say: "the fullest co-operation of the banks in the current Canada Savings Bonds drive." Now, my question is: are you paid a commission on the sale of these bonds?

Mr. PATON: Yes, we are, sir.

Mr. LIND: Then why would you not co-operate if you are making money on it?

Mr. PATON: I might point out, Mr. Lind, that there are new subscriptions for Canada Savings Bonds which are actively sold by banks. In many cases it means withdrawals from savings accounts, held by these banks and this affects them. It is this feature which should be given quite careful consideration when we refer to the co-operation the chartered banks give to the government.

Mr. LIND: I am sure you would have to admit that Canada Savings Bonds were a less risky type of security than having a deposit in one of the eight chartered banks, would you not?

Mr. PATON: I would say that neither one carried any risk whatsoever.

Mr. LIND: You go on to explain how you are co-operating with the Dominion of Canada by selling Expo passports. Do you receive a commission for selling these Expo passports?

Mr. PATON: Yes, sir, we receive a commission. That is correct.

Mr. LIND: I am now going to the statement on page 5—

Mr. PATON: I should add, Mr. Lind, that the commission in all these areas is not net to the banks. We have costs apropos of advertising and publicity to let people know we are in both businesses referred to, so the commission which we receive is not a net gain by any means.

Mr. LIND: But you are paid a commission?

Mr. PATON: Yes.

Mr. LIND: That is the point I wanted to make.

On page 5 you make the statement: "Uniformity of action was therefore essential and was achieved through study, research and discussion carried on through the association". You are referring up above to the uniformity of procedures. Who was this study made for; was it made for the eight chartered banks or in their interests?

Mr. PATON: This was made by the committee of the association which is comprised, as normal committees, of representatives knowledgeable in a particular field from each bank in which they are joined by one of the association staff themselves.

Mr. LIND: But this information was for the use of the eight chartered banks only?

Mr. PATON: What page on the brief are you referring to. Is it page 5?

Mr. LIND: Yes, page 5.

The CHAIRMAN: While this page in the brief is being turned up I might say to Mr. Lind that even after taking account of various interruptions, your time is just about gone.

Mr. LIND: I just have one more brief question here.

Mr. PATON: That reference to uniformity of action—that is why I wish to refer to it, Mr. Lind—has specific association with the magnetic ink system, the M.I.C.R. encoding of cheques. Obviously if there had been various systems in effect in the banking profession thought the banking community there would be some havoc raised. So it was necessary to have a uniform approach made and this was a typical example. That is what the word uniformity is referring to here.

Mr. LIND: I have one further question, if I may, Mr. Chairman, and this goes over into the area of C.M.H.C. mortgages. I think you made a statement something along this line, Mr. Paton, the other day, that if the ceiling is lifted it would allow the banks to compete for additional deposits and if they can get these deposits they will go into N.H.A. mortgages. You made a further statement that there is only so much money in the country. Where would you be getting these additional deposits?

Mr. PATON: In the deposit field we would be getting them from other institutions. We would be getting them intra-bank—from one bank to another as we compete—and also from competing deposit institutions, which are not chartered banks.

Mr. LIND: As the eight chartered banks and their associated trust companies control 82 per cent of all the deposits in Canada today, do you not think that you control a fair degree of the money supply in Canada?

Mr. PATON: I think I have some figures somewhere, Mr. Lind, which would be interesting in that regard. I do not think the figure of 82 per cent is correct.

Mr. LIND: As I may have mentioned, the Governor of the Bank of Canada said that the chartered banks represented 73 per cent plus the five major controlled trust companies—we gave them the benefit of the doubt—controlled 11 per cent.

Mr. PATON: You assumed that the banks—

Mr. LIND: The banks control, either directly or indirectly.

The CHAIRMAN: Do you mean 11 per cent of the deposits?

Mr. LIND: Yes.

Mr. PATON: I think, perhaps, the 73 per cent figure is the figure which we should stay with and discuss. I think it is, perhaps, an unwarranted or unreasonable assumption to attach any shareholding, whatever it is, in a trust company and relate to that, similar control which the individual bank would have over that trust company's deposits. I do not agree with the combining of the two.

Mr. LIND: Would you like me to go into a specific example?

The CHAIRMAN: Ordinarily, I would invite you to do that, Mr. Lind, but I think your time for questioning has expired.

Mr. LIND: I have just one further question on that subject.

The CHAIRMAN: Order.

Mr. LIND: If they can get these deposits, the banks may go into the N.H.A. mortgage field. I would like a definite statement whether the banks are going into the N.H.A. mortgage field and whether they can entice these additional deposits or not, before we give consent to lift the ceiling off the interest rate.

The CHAIRMAN: Mr. Paton, could you or one of your colleagues answer that question?

Mr. PATON: In all of our comments and speeches, Mr. Lind, and in individual discussions, the association, as a group, have indicated their appreciation and pleasure in having freedom to go into mortgage lending. It automatically follows that we will go into that field to the best of our ability. Once again, this will be a decision for each bank, in connection with its assets mix as it has been referred to on a number of occasions, but there is no doubt in my mind that with the freedom given to the banks to participate in this form of lending, there will be a larger pool of funds available for this type of financing.

The CHAIRMAN: I will recognize Mr. Langlois next, followed by Mr. Caouette and Mr. Johnston. I would assume, unless somebody indicates right now, that after the people I have mentioned are finished their questioning, we will have concluded our first round of questioning. Do you have your name down, Mr. Flemming?

Mr. FLEMMING: No, but I would like to be included in the list.

The CHAIRMAN: You have not had an opportunity yet?

Mr. FLEMMING: No, not yet.

The CHAIRMAN: I am sorry. I will add your name as well.

Mr. LANGLOIS: Mr. Chairman, I have a few questions here following some of the statements given by the witness on this latter part of the questioning. I also have a few on the brief which was presented. On page 2, at the bottom of the



page, you mentioned that the 6 per cent interest rate affects the chartered banks and the Quebec savings banks and that it does not affect the other institutions or financial societies which go into the lending business. Now, this 6 per cent which the chartered banks are now charging is the maximum rate which they can collect now on loans under their present charter. The other institutions do not have a similar charter. Under your charter, that is to the effect, if you want to call it in theory, you are permitted to have loans 12 and a half times the reserve which you have in the Bank of Canada at the moment. Now, am I correct to state—this is the figure which the Governor of the Bank of Canada gave—that approximately the reserves of the chartered banks with the Bank of Canada were \$1,090 million at the moment? Is that correct?

Mr. PATON: That is approximately right.

Mr. LANGLOIS: In theory, this is a net reserve. This is not only savings accounts. You must have some other form of assets which could be considered in there at the same time, I imagine. At any rate, the total reserve is \$1,090 million. If we take for granted that this total reserve would be savings accounts deposits at an average of 3 per cent interest, it would mean approximately \$33 million which you would be paying out in interest and when you multiply this \$1,090 million it gives you a total of permissible loans—and I want you to correct me on that if I am not within the figures—of something like \$13,625 million, using the rate of 8 per cent. I am going to ask you this question. Do all the savings accounts in the chartered banks go into your federal reserves in the Bank of Canada reserves?

Mr. PATON: In computing out 8 per cent legal reserves, Mr. Langlois, it is based on the Canadian deposit liabilities of the chartered banks which includes savings accounts, demand deposits, notice accounts, the whole conglomeration.

Mr. LANGLOIS: Bonds?

Mr. PATON: No, this is on the liabilities side.

Mr. LANGLOIS: Yes, the liabilities, but this constitutes your reserves?

Mr. PATON: The 8 per cent figure is arrived at by taking 8 per cent of the total of these for the entire banking system. Each individual bank has its proportion.

Mr. LANGLOIS: I will give you a specific example. I deposit in your bank \$100; do you take \$8 out of it as a reserve for the Bank of Canada or do you take the whole \$100 and send it there as a reserve?

Mr. PATON: Perhaps, with your permission, Mr. Chairman, I might ask Mr. MacIntosh who was answering questions which someone asked along similar lines the other night, Mr. Langlois, and I hope he would be able to answer you.

Mr. LANGLOIS: What I would like to get established by this, sir, is the difference between yourselves and the other banks or other financial institutions not under the same charter; I want to find out the difference.

Mr. PATON: They have no statutory reserve as we have. Our reserve consists of the basis I gave yesterday.

Mr. LANGLOIS: Would Mr. MacIntosh care to answer this question on my latest example. When I deposit \$100 in to a savings account do you take the total \$100 as a reserve or just \$8 out of that \$100?

Mr. MACINTOSH: Just the \$8, Mr. Langlois.

Mr. LANGLOIS: Out of the \$100?

Mr. MACINTOSH: Yes. May I add that some other bank has lost the \$8, through the \$100 deposit to us and, therefore, reduces its reserve. There is no change in the system. It is a shift from one bank to the other.

Mr. LANGLOIS: Yes.

Mr. MACINTOSH: If we gain in the clearing \$100 by reason of your taking a deposit from bank A and putting it in bank B, then there is merely a readjustment of who has the cash and who has the deposit liability. There is no change in the amount of cash reserves in the system nor any change in the total amount of deposits. It only moves from one to the other.

Mr. LANGLOIS: Where do you get your commission on loans? You agree that you do not lend your depositors' money.

Mr. MACINTOSH: Oh, yes, we do, sir. We lend our depositors' money within the limits of the 8 per cent and further liquidity requirements of the banks.

Mr. LANGLOIS: How come the Governor of the Bank of Canada stated you cannot because it does not belong to you, it is a liability.

Mr. MACINTOSH: Our liabilities to our depositors are matched on the other side of the balance sheet by our assets. We are paying interest on our liabilities and we are earning interest on our assets. We hope that there will be a spread between.

Mr. LANGLOIS: But according to the figures which I gave, this is a liquid reserve of \$1,090 million.

Mr. MACINTOSH: But sir, it is not liquid in the sense that it is available to us. It is required that we keep it there at all times. If I might refer you to the table which the Governor of the Bank of Canada presented last week to the Committee and which I use by reason of the fact I think all the Committee members have those figures available to them, you will see there that the total Canadian dollar liabilities of the Canadian banks at December 31, 1965 were \$19,022 million.

Mr. LANGLOIS: \$19,022 million.

Mr. MACINTOSH: Mr. Chairman, would it help, perhaps, if there were copies of this distributed. May I ask if there are any extra copies?

The CHAIRMAN: It seems to me they were distributed.

Mr. LANGLOIS: Yes, but I do not seem to have it with me. I have the other statements but I do not seem to have that one.

The CHAIRMAN: Perhaps you left your copy here or perhaps one of the members will lend Mr. Langlois his copy so we can move right along. The clerk will provide Mr. Langlois with a copy.

Mr. LANGLOIS: Yes, I have a copy here. This was December 1965?

Mr. MACINTOSH: Yes, sir, on the first page you will see there that the total Canadian dollar liabilities of the banks are \$19,022 million.

Mr. LANGLOIS: Yes.

Mr. MACINTOSH: The cash reserves of the banks, the first item in the assets, are \$1,417 million. The ratio of the first item to the last is approximately 8 per cent. It may be fractionally different from that, of course, because of the fact

that we take our 8 per cent average on a monthly average basis and I presume these statistics relate to one single day, December 31. But the ratio, as you will see there, is approximately 8 per cent, from \$1,400 million to \$19 billion.

Mr. LANGLOIS: When you are talking about this 8 per cent, do you mean that it is 8 per cent of your deposits or should you have 8 per cent of your loans?

Mr. MACINTOSH: We mean 8 per cent of our deposits, sir.

Mr. LANGLOIS: You are spending 8 per cent of your deposits and not keeping in reserve the total of 8 per cent which you have as loans outside?

Mr. MACINTOSH: No, it is 8 per cent of the deposits which is the requirement, Mr. Langlois, not of loans. The amount which is in loans and mortgages and securities of all kinds is the difference between the sum of total liabilities less the amount which is held in cash reserves by law.

Mr. LANGLOIS: If you have \$1,090 million in reserves which constitutes 8 per cent of your savings deposits and everything else that could be included, you have to multiply that by  $12\frac{1}{2}$  per cent to come up to your total loans on the other side?

Mr. MACINTOSH: No, sir; I think if you will look at the table you will see that it balances precisely and that the assets must equal the liabilities and that the difference between the cash reserves of \$1.4 billion and the total liabilities of \$19 billion consists of different kinds of earning assets, of which \$13 billion are in loans and a further \$4 billion in securities and another \$500 million in miscellaneous assets. So, the requirement to keep a cash reserve of 8 per cent, leaves us only the difference of 92 per cent available for earning assets.

Mr. LANGLOIS (*Mégantic*): This is the \$92 that you lend out?

Mr. MACINTOSH: This is the \$92 that is in our earning assets that we lend out or hold in the form of securities, that is right.

Mr. LANGLOIS (*Mégantic*): When I go to your bank and deposit \$100, and my friend comes in and borrows \$100, my account does not go down \$100, it stays exactly the same.

Mr. MACINTOSH: You are assuming that your deposit comes newly into the system, but this is an impossibility. For instance, in the figures with which we are dealing here, it is impossible for the banks' total liabilities to rise from \$19 billion to, shall we say, \$20 billion because of the fact that we would fall short of our 8 per cent cash reserve. We cannot go below the 8 per cent, and there is no way in which the banks, individually or in total, can expand that deposit figure.

Mr. LANGLOIS (*Mégantic*): I am not talking about that. Your cash reserve is 8 per cent, but your loans are not necessarily cash.

Mr. MACINTOSH: No, the loans are earning assets and not in cash. That is correct.

Mr. LANGLOIS (*Mégantic*): This is where you are lending out on credit extension. This is where the chartered banks are empowered to create this credit.

Mr. MACINTOSH: I would take exception to the use of the word "create" in this sense. If you mean to say that we are granting credit when we make loans, we certainly are, as are all the other institutions who are included in the table.



Mr. LANGLOIS (*Mégantic*): Yes, that is quite true, but then you are not lending out the other customer's money.

Mr. MACINTOSH: Oh, I think we are. Under the present circumstances when there is a tremendous demand for loans, I am sure we would be very glad if we were able to expand our loans without limit, and simply manufacture them out of whole cloth, but I am afraid that is virtually impossible.

Mr. LANGLOIS (*Mégantic*): What is your limit, then? Is it your eight per cent reserve?

Mr. MACINTOSH: Yes; it is impossible for us to lend more than we now have, given the level of deposits which we have, and that level of deposits cannot be expanded so long as our cash reserve is \$1.4 billion—I am using these figures as of last December—and the control of that figure rests solely with the Bank of Canada. It is not in our power to make the Bank of Canada change it. We cannot go and sell assets to the Bank of Canada unless they choose to buy them.

Mr. LANGLOIS (*Mégantic*): With that I agree, but your total 8 per cent reserve is the control that the Bank of Canada has on the chartered banks on the over-all picture.

Mr. MACINTOSH: That is correct.

Mr. LANGLOIS (*Mégantic*): That is the focal point.

Mr. MACINTOSH: That is correct.

Mr. LANGLOIS (*Mégantic*): According to the Governor of the Bank of Canada, not the present one, but Mr. Towers—you cannot lend anybody else's money. I am depositing into your bank, but you are not lending it out. You are lending your credit on the basis I deposit there. That is all right, because you have to take 8 per cent of that and send it out to the Bank of Canada, do you not?

Mr. MACINTOSH: We are a financial intermediary type of institution. Like all financial intermediaries we, in fact, do interpose between borrower and lender, and we are definitely lending other people's money. We are borrowing, and we are lending. We are borrowing people's money and then lending it to borrowers. We lie between borrowers and lenders as do all financial institutions in one form or another. This is *altroue de caisse populaire*, trust companies, loan companies, insurance companies and anything you care to name. They are all financial intermediaries between borrowers and lenders.

Mr. LANGLOIS (*Mégantic*): But they do not all have the same charter.

Mr. MACINTOSH: No, but they all have a cash reserve requirement of some sort. In our case they happen to be more severe than in the case of other near banking institutions, as you will see if you refer—

Mr. LANGLOIS (*Mégantic*): What do you mean by being "more severe"? Do you feel that 8 per cent is too high a reserve?

Mr. MACINTOSH: Yes, we do, indeed, and the new act proposes to alter that reserve ratio. If I may refer you to the second page of Mr. Rasminsky's table, you will see that at the top right hand corner of the page where we have the trust companies' figures the cash reserve of the trust companies is 2.9 per cent of their deposit liabilities, as opposed to our 8 per cent.

Further down the page you will see the mortgage loan companies cash reserve ratio is 2.2 per cent.

Turning over to the next page, in the case of the *caisse populaire* and credit unions, the figure is 11.1 per cent, cash on hand and on deposit, as a ratio of the total assets or, if you like, the total liabilities.

So each institution has to keep a certain amount of cash reserves either by law or by conventional practice and, of course, our position is that our cash reserve ratio has been higher than necessary and, moreover, it earns no interest at the central bank; whereas in the case of all these other near banking institutions they, in fact, make their deposits not free of interest to the central bank, but at chartered banks or other institutions where they earn interest. So the inhibition on their power to take liabilities and pay interest on them is not as great as in our case.

MR. LANGLOIS (*Mégantic*): Could you give me approximately what your total loans—

THE CHAIRMAN: Mr. Langlois, I just want to say at this point that the twenty minute period has expired, but I want to let you ask this question and get the answer.

MR. LANGLOIS (*Mégantic*): What are the approximate total loans at the moment, the overall picture, in the chartered banks?

MR. MACINTOSH: The latest available figures are those published by the Bank of Canada on November 3, and relate to our loans on October 26, 1966, at which time the total general loans of the banks—I would have to add up these items. They are broken down into different categories here. They are in the order of \$13 billion, sir.

MR. LANGLOIS (*Mégantic*): That is what I had a while ago, \$13,625 million multiplied by  $12\frac{1}{2}$ . I am using that on the basis of the Governor of the Bank of Canada's statement, \$1,090 million. And you are collecting interest—I am just giving out these figures—on these loans at 6 per cent to give you \$817.5 million collectible interest.

MR. MACINTOSH: Mr. Langlois, if we were able to multiply by twelve and a half times the amount of our loans, we would then have total assets in the banking system of around \$150 billion. If you will look at the figures here you will see that—

MR. LANGLOIS (*Mégantic*): No, I am talking about your reserve, your \$1,090 million reserve, and this is where I got this \$13,625 million that you mentioned was approximately \$13 billion. This would be your loans at 6 per cent, approximately—you may have a few lower than that; I have not found them yet—that will give you \$817.5 million gross revenue on that interest.

Now, if you figure out the total interest loss at 3 per cent on your \$1,090 million or, as this is all reserve this would be all in savings accounts, the maximum interest you would be paying at 3 per cent would be \$33 million. Now, if you want to find out the difference between the two, you have to subtract them.

MR. MACINTOSH: Well, sir, if you want to find out the difference between the two, I would suggest that the most convenient place to go is the consolidated earning return of the chartered banks, which appears also in the form of Schedule Q, I believe, in the Bank of Canada's statistical summary at each year end. If what you are driving at is the amount of earnings in relation to expenses, then—

Mr. LANGLOIS (*Mégantic*): I did not mean the amount of total expenses. I just took one sector of the expenses that you will be paying interest on to the depositors at an average of 3 per cent, on the reserves that you are not getting anything back on. You do not receive anything on that one, because you told me the Bank of Canada do not pay any interest on deposits, on the reserve.

Mr. MACINTOSH: The interest which we paid in 1965 on Canadian personal savings deposits was in the amount of \$235 million. These figures you can find in Schedule Q of the Bank of Canada statistical summary.

The CHAIRMAN: If I may interrupt again here, I realize that Mr. Langlois is proceeding in a very interesting area, with which we have been dealing one way or another to some extent already, and perhaps he may want to return to it when next there is an opportunity. But I think in fairness to the others we should proceed to the next one on the list.

Mr. LANGLOIS (*Mégantic*): Mr. Chairman, I might say here that I wish you had been in the chair the other day when there was an hour and a half on the same question.

The CHAIRMAN: That is true, but if this is the error of the Chairman or the Acting Chairman, they must assume responsibility and I am sure that most of us will agree that this error should not be repeated. It would be very unfair to everybody, especially to whoever is in the chair.

Mr. LANGLOIS (*Mégantic*): May I ask you this question. When we do come back, if I have it right sir, on the general questioning I will still be able to maintain the general questioning before we take any specific case.

The CHAIRMAN: No, not before—after.

Mr. LANGLOIS (*Mégantic*): What do you mean by “after”?

The CHAIRMAN: I suggested to the Committee that once we finished our first round, so that everybody on the Committee, including the other participants who are interested, has an opportunity for general questioning, we would then proceed to question the association on their brief section by section. Now, obviously if what you are interested in pertains to one of the sections and is easily related then there would be no intervention by me. But, even if it is not once we finish going over the brief and the supplementary documents presented, then if you feel that you have not covered this area which you are discussing, why obviously you will have a further opportunity. Is that all right? You need not be concerned that this matter, which understandably is of great interest to you and others as well, will be cast aside without being adequately ventilated. In using the word I did not imply any judgment of any kind.

Mr. LANGLOIS (*Mégantic*): I hope not.

The CHAIRMAN: No. It is just a question of—

Mr. LANGLOIS (*Mégantic*): Because I could do a little bit of exterminating myself?

The CHAIRMAN: That shows how careful we must be in the use of language delivered to an assembly of this type.

The next questioners I have are Mr. Caouette and Mr. Johnston. I mention those names, feeling that there were no formal members of the Committee who



had wished to pose questions. I do not want to create any controversy. I just wondered as between Mr. Flemming and Mr. Caouette, whether you would like to defer to Mr. Flemming or whether Mr. Flemming would mind having Mr. Caouette proceed.

Mr. FLEMMING: Mr. Chairman, I would not want to disturb the sequence you just announced. I would yield to Mr. Caouette and Mr. Johnston even though—

The CHAIRMAN: They are working members.

Mr. FLEMMING: That is quite all right.

(Translation)

Mr. CAOINETTE: Thank you, Mr. Chairman and Mr. Flemming. Mr. Chairman, what astonishes me is the annoyance or the obstinacy of the banks and their representatives who insist that the chartered banks, the savings banks and the Caisse Populaire are the same sort of thing. They say there is no difference among them. The savings banks however lend mainly to small people who are not in business, whereas the chartered banks are engaged in the commercial field. And what astonishes me also, is when I hear Mr. MacIntosh, who is an economist of the Canadian Bankers' Association, maintain that there is no credit creation taking place at the level of the chartered banks, that it is simply an expansion of credit. Might I know what is the real difference between credit expansion and credit creation?

(English)

The CHAIRMAN: Which of you gentlemen would like to handle that one?

Mr. PATON: I shall defer to Mr. MacIntosh.

Mr. MACINTOSH: Mr. Caouette, may I say for the record that I am not an economist of the bankers' association. They have not seemed fit to hire me for that purpose.

Mr. CAOINETTE: You act as one.

The CHAIRMAN: You are part of the delegation but you are actually employed by the—

Mr. PATON: Mr. MacIntosh's title is Joint General Manager of the Bank of Nova Scotia, for the record.

The CHAIRMAN: It is not unusual to find somebody with the name of MacIntosh working for the Bank of Nova Scotia. You may proceed, Mr. MacIntosh.

Mr. MACINTOSH: Mr. Chairman, there are a few Scotsmen left.

The reason that I prefer to talk about credit expansion, Mr. Caouette, is that I think in the context in which the phrase "credit creation" has been used in this Committee meeting there is an unfortunate implication that the banks have some power to create money which is not the case and, therefore, I think it is preferable to talk about expansion of credit.

(Translation)

Mr. CAOINETTE: All right, Mr. MacIntosh. In the Canada Year Book for 1963-64, page 1195, we read: "The principal means which the Bank of Canada uses to influence the level of cash reserves in the chartered banks...is the

purchase sale of government securities". Suppose the Bank of Canada today buys one billion in federal government bonds. Do the chartered banks have the right, following this purchase, to lend this billion dollars  $12\frac{1}{2}$  times? Do they, or do they not? I do not want to listen to any rhetoric or philosophy, is it just yes or no?

(English)

Mr. MACINTOSH: I am afraid I cannot give the "no" answer to a complicated monetary question, Mr. Caouette. If the central bank chooses to expand the amount of cash reserves in the system by reason of purchasing securities in the open market, in the first place one has to keep the figures in proportion to the size which would actually be relevant. Cash reserves, as we said a short time ago, are approximately \$1,500 million. The bank of Canada might see fit to expand those reserves at the rate of shall we say 6 or 7 per cent per annum which is somewhat less than—well, shall we say, \$100 million per annum at the present time. Now, if over the course of a year the cash reserves of the banks were to increase by \$100 million, then it would be the case of through the process of expansion and as long as the banks were able to hold their share of this increase in deposits they would eventually have assets and liabilities which would be approximately  $12\frac{1}{2}$  times the original injection of cash by the central bank and it would be up to the central bank to put this process in motion or to stop it or to reverse it. No single bank would be in the position to change it or would the system be able to change it without the judicial decision by the central bank that it should be done.

(Translation)

Mr. CAOINETTE: I understand that a particular bank may not be able to do it, but through the Canadian Bankers' Association you can carry that out. I emphasize this point. When the Bank of Canada buys Government bonds, this purchase makes it possible for the total banking system to multiply by  $12\frac{1}{2}$  times the amount that the Bank of Canada originally purchased, yes or no?

(English)

Mr. MACINTOSH: It would be possible for the banks assets and liabilities to eventually expand by  $12\frac{1}{2}$  times, but it is also possible for the near banks' assets to also expand if they acquired some of the increased cash that then goes into the system. When it is not exclusive to the chartered banks and if a trust company or a credit union—

(Translation)

Mr. CAOINETTE: Could a Caisse Populaire do the same sort of thing?

(English)

Mr. MACINTOSH: Oh, yes.

Mr. CAOINETTE: Oh, no.

Mr. MACINTOSH: Oh, yes, indeed. Let us take, if we may, the case of a caisse populaire acquiring some cash—

(Translation)

The CHAIRMAN: I think that you should allow the witness to finish his answer, Mr. Caouette.

(English)

Mr. MACINTOSH: Mr. Caouette, if a *caisse populaire* acquired cash it does so through the process of attracting deposits. Those deposits are held initially in the form of cash. Now, if it were able to make a loan with the cash it has acquired, and if the borrower withdrew all the cash in the loan, then the *caisse populaire* could do nothing else nor could a chartered bank. It is the same thing. But, if the *caisse populaire*, having made a loan to the customer and given him a credit on its books, found it had not lost cash because it was able to continue to attract deposits it would be able to go on expanding its loans as well because the *caisse populaire*, just like a bank, would not be actually lending cash unless people took cash out. They do not do that. If you will look at the balance sheet of the *caisse populaire* you will see that it is almost identical in structure to that of a chartered bank. The reason that they continue to make loans as we do is that they find by experience as we do they do not need all cash. In fact they have 11 per cent against our 8 per cent. They are earning interest on their 11 per cent and we are not.

● (12.50 p.m.)

(Translation)

Mr. CAOUPETTE: So the law provides that the chartered banking system does have the right to multiply by  $12\frac{1}{2}$  times the amount of bonds purchased by the Bank of Canada. I would draw attention to your previous reply to Mr. Langlois, to the effect that the banks lend their deposits.

In 1939, the former Governor of the Bank of Canada, Mr. Powers, was put this question: "Do you understand whether the banks can lend what does not belong to them?" "Obviously," said Mr. Powers, "the banks cannot lend the money of their depositors." Well, he was not accurate then, because you can see this at page 445 of the report of the Banking and Commerce Committee. In answer to another question, Mr. Powers said there is no doubt at all that the banks do create this medium of exchange which is called credit. This is the Governor of the Bank of Canada speaking. This is why banks exist; that is the very nature of banking operations, just as the function of a steel plant is to produce steel. The process is to make a book entry, that is all, it is a creation. So, how is it that you maintain that is not a creation?

(English)

Mr. MACINTOSH: Mr. Caouette, I would not want to be in the position of commenting on the views of a distinguished governor of the Bank of Canada of the past. I would merely draw your attention to the fact that a chartered bank is a financial intermediary, which is no different from any other financial intermediary. I have just given you an instance of a *caisse populaire* which acquired deposits, in the process of paying for them, from the public, and if the *caisse populaire* were to find that having acquired deposits they were all withdrawn in a cash form, it too would not be able to expand its loans, and it is able to expand its loans because it finds that it does not lose all its cash. The reason it does not lose all its cash is that it is paying a competitive rate for deposits sufficient to keep cash coming in. It finds that its sum total of all depositors are not withdrawing all cash at once. If they were to do so, the *caisse*, like any financial institution, including a bank, would have to contract. In fact it would be unable to meet its obligations if the general public were to demand at one and the same moment cash entirely.



If you are implying there is something peculiar and unique about the power of a bank to create credit, this is not the case. The banks are no different from any other institution except that the process is initiated through the fact that the central bank controls the cash reserve and, as Mr. Rasminsky said here the other evening, the process of monetary control spreads through the whole financial system beginning with the banks, but not ending with them.

(Translation)

The CHAIRMAN: Could I interrupt for a moment? I realize it is nearly one o'clock and I wonder if we might well adjourn and continue your questions this afternoon?

Mr. CAQUETTE: Yes.

Mr. GRÉGOIRE: May I make a suggestion. It seems there is some confusion, and that we need some additional information. Could we have a representative from the caisses populaires or the savings banks here to get his point of view before the banking Committee?

The CHAIRMAN: I will pass this suggestion to the steering committee and they can report to the full committee. So far, the caisses populaires have not expressed any wish to attend our meetings.

Mr. GRÉGOIRE: Could we ask them to send a representative?

The CHAIRMAN: I will pass your suggestion on to the steering committee and they will report to the full session of the committee. I declare this Committee adjourned until 3.45 this afternoon.

#### AFTERNOON SITTING

The CHAIRMAN: Gentlemen, I see a quorum and I now call the meeting to order.

● (3.50 p.m.)

(Translation)

Mr. Caouette, you have the floor.

Mr. CAQUETTE: Thank you, Mr. Chairman. At adjournment time, at noon, Mr. MacIntosh was telling me that no credit was actually being created by chartered banks in this country. Now, this morning, I quoted an example to the effect that the Bank of Canada would buy, shall we say, various Government securities in the amount of one billion dollars. This increases by a proportionate amount the chartered banks' reserves. Mr. MacIntosh answered me at that time that even then money was not actually being created.

In spite of all the respect he had for the former Governor of the Bank of Canada, Mr. Powers, he added that he would deny the fact that the banks create money or scrip money, if you prefer. As it happens, there is a letter here from the Bank of Nova Scotia signed by its president, Mr. Nicks, and dated August the 23rd, who comments on the newsletter of the Royal Bank of Canada which was already quoted here. Mr. Nicks said: "The study of the financial and banking system is a very complicated and difficult matter". I will certainly not deny that, it is even difficult for the banks themselves. However, we do feel that the newsletter of the Royal Bank does describe very accurately the fundamental mechanism of the creation of money.

There is a bibliography here which people interested in the subject can consult. Mr. MacIntosh, this morning, also spoke of the cost of money. This would apparently explain why the banks have asked for a removal of the 6 per cent ceiling.

If you find one billion dollars is too much, it would have a dangerous inflationary effect since chartered banks enjoy the power to multiply that reserve by twelve and a half, but be it as it may, when the Bank of Canada buys a security, this constitutes a reserve, this allows you to multiply by twelve and a half times your original reserve, this allows you, in other words, to create credit to the extent of several billion dollars.

What is the cost of that money which the banks may create from this reserve organized by the Bank of Canada? How much does that credit cost?

(English)

The CHAIRMAN: Which of you gentlemen would like to deal with that question?

Mr. R. M. MACINTOSH (*Joint General Manager, Bank of Nova Scotia*): Mr. Caouette, naturally I never disagree with my president, either in public or in private.

Mr. CAOINETTE: So you admit the creation?

Mr. MACINTOSH: No, I have not finished what I was going to say. You appreciate that the draft reply to the letter was written originally in English. I would have to say that I do not think in the process of translation into the reply to Mr. Grégoire that the words were used which I would have used. I do not suppose our translator is fully qualified in monetary theory and therefore the use of the language I would question seems to me to be a semantical problem and the word "creation" in English has a connotation which I insist is not appropriate under the circumstances.

When the Bank of Canada initiates an expansion of credit in the system it buys securities. The cheque which it issues to the seller of the securities is deposited in a chartered bank by the seller. The chartered bank thereupon redeposits the cheque on its account at the Bank of Canada. At that point the bank has cash and it has a deposit in equal amount. The bank may then make a loan to a customer and in doing so the customer will normally take a deposit rather than draw cash.

If the customer were to draw cash the bank would therefore be unable to do any more than lend the original amount of money which it got on deposit by reason of the original open market transaction of the Bank of Canada. The only reason the bank will be able to further expand its deposits and loans eventually is by reason of the fact that it will attract back funds arising out of loans made either by itself or other banks and in the process of competitively attracting deposits it will be possible for it to further increase its loans. But, the process of credit expansion which I am speaking of is not peculiar to the banks. It is identical in the near banks and I would like to call your attention to a speech which the Governor of the Bank of Canada has just published and which has come to our attention today. It was given yesterday in Rome, in which he describes the process by which the central bank operates in controlling the

credit conditions of the economy, and in which he takes account not only of the volume of deposits in the banking system but the volume of liabilities held by the near banks.

*(Translation)*

Mr. CAQUETTE: You make no difference between near-banks, Caisses populaires, savings banks and chartered banks, but one can well admit that,—I have founded a Caisse populaire in Rouyn-Noranda, I was a member of the founding group—before this Caisse populaire can make a single loan it will first of all have deposits, it is unable to loan if it has no deposits, whereas a chartered bank may loan money, will loan money and have deposits thereafter.

For instance, I can go to the Bank of Nova Scotia tomorrow, apply for a loan of 100 thousand dollars and after providing the proper security to the bank, turn over my wife, my children, my insurance policies and what have you, I am granted a loan of 100 thousand dollars which I did not have before. There is not a single account which has been reduced in the bank, and I will walk out of that bank with 100 thousand dollars in new credit, which you will add to the other deposits you have there, because I will leave the 100 thousand dollars with you. You will have to admit that at this time you only have 5 per cent cash compared to all the transactions carried out in this country, 95 per cent of which are done through credit money. There are two kinds of money, first we have coins and bank notes and then, we have credit. You will admit that?

*(English)*

Mr. MACINTOSH: The definition of the money supply in the country would properly include the deposits of the chartered banks, the currency in circulation, the deposits of near banking institutions which are of a banking character. I am very glad that in your work in connection with the Caisse populaire you have been able to recognize that you can only lend what you can get on deposit. We feel the very same way about the process in banking circles and there is, in fact, no difference whatever.

Mr. CAQUETTE: But you lend more than the deposits.

Mr. MACINTOSH: May I refer you then to the balance sheet of the Caisse populaire which we were talking about this morning. Now, if you will look at page 3 of the statistics produced by the Governor of the Bank of Canada last week you will see that in these statistics the cash reserves of the Caisse populaire are 11.1 per cent. I might say in further elaboration of something I said this morning that this combined balance sheets of the credit unions and Caisse populaire have not been completely consolidated and there is some double counting of their cash reserves. The Governor of the Bank of Canada referred to this last week and in fact he mentioned that the cash reserves of the caisse are in the order of 5 or 6 per cent rather than 11 per cent, because a good deal of the deposits of the caisse are deposited with their centrals or with each other. Now, if I use the same language that you use I would have to say that the Caisse populaire with a 5 per cent cash ratio are able to expand their loans to the extent of 20 times over their cash. If you wish to use the same language, that is the result that you get. If you refer to the trust companies which have a cash reserve of 2.2 per cent, then it is only reasonable for you to say that the trust companies



are able to expand their deposits and loans to the extent of 40 times their cash reserve.

I do not think there is any distinction whatever and there certainly is not in the minds of any monetary economist in this country or in any other.

(Translation)

Mr. CAOUPETTE: But according to you, Mr. MacIntosh, if the Caisse populaire were to buy securities from the Bank of Canada, would it have the same power of expansion as the chartered bank has?

(English)

Mr. MACINTOSH: When a chartered bank buys a security from the Bank of Canada, this does not expand our power to take deposits. On the contrary, Mr. Caouette, it uses up some of our deposits.

(Translation)

Mr. CAOUPETTE: If the Bank of Canada buys securities from the Government this increases your reserves, but it does not increase the reserves of the Caisse populaire?

(English)

Mr. MACINTOSH: It can indirectly, yes.

(Translation)

Mr. CAOUPETTE: Yes, but only through the chartered banks?

(English)

Mr. MACINTOSH: The process only begins with the central bank purchasing securities. If the seller of the securities puts his money in a Caisse populaire, the same process takes place, exactly.

(Translation)

Mr. CAOUPETTE: Obviously, but he has to start with the chartered banks?

The CHAIRMAN: The Clerk has just informed me that you have already had more than 20 minutes.

Mr. CAOUPETTE: Thank you, Mr. Chairman.

(English)

The CHAIRMAN: I recognize Mr. Johnston followed by Mr. Latulippe.

Mr. JOHNSTON: Thank you, Mr. Chairman. The line of questioning that I have will follow along with what Mr. Caouette has been talking about, but I would like, if possible, to return to the summary balance sheets of selected financial institutions. Perhaps the picture could be made a little clearer for me. In some ways listening to this morning's discussion, I almost had the idea we were working with a closed system, but on looking at the balance sheet, I see that between December 1960 and December 1965, the cash reserves has been increased, and we have the figure, of \$992 million and the increase to \$1,417 million in the five years time. I think this was explained partially in the answer to Mr. Caouette, how is this done, how does the increase come about?

Mr. MACINTOSH: Mr. Johnston, this is a process which takes place over considerable periods of time and at low rates of growth. If you try to look at the system as though you were taking a still photograph, let us suppose to the literal

that you take a still photograph of a baseball player sliding into home base and you have a still photograph when he starts and a still photograph when he gets there. You only have two pictures, when he started and when he finished, and you say "what happened? Is it by some magic that he got from one place to another?" No, it is only because you have a photograph at the beginning and the end of the time and it does not show the process by which he slid into the base. To do that you would have to have an instantaneous series that shows every transaction. I hope the analogy has some relevance here, because what I mean to say is that this is a process of expansion that goes on, and if you look at the photographs in 1960 and the photographs in 1965 and you say how does this come about, all I can say is that there is a process going on, just as there would be from one still photograph to another.

Mr. JOHNSTON: But there must be some mechanics of this process that could be phrased in less picturesque language.

Mr. MACINTOSH: All right; let us go back over the mechanics. The central bank buys securities. We used the instance the other day of purchasing \$8 millions in securities from a seller. The seller is a private party in Canada who deposits the money in a bank; the bank re-deposits the cheque in the Bank of Canada, and there has been an increase on both sides of the balance sheet of the system of \$8. Now if there is one bank only in the system—and you must understand the nature of this assumption—then at the time when that bank, having acquired \$8, makes a loan, and the person who borrows the money chooses not to take out cash, but to accept a deposit at the bank, then the person who had borrowed the money pays the money that it has on deposit to another person and that person, who is a recipient of the funds, deposits the money back in the same bank, because there is only one bank in my assumption. You now have a situation in which loans have gone up a further \$8 million and deposits have now gone up \$8 million and the bank still has cash. The system hinges on the fact that most depositors do not want cash at any one time; the bank would then find it possible, by a gradual process of expansion, to create further loans to make loans to customers which would lead to the establishment of deposits in the event that the borrower did not choose to draw out cash.

If you expand that bank into a total system, the problem which an individual institution has in that system, whether it is a bank or a near bank, is to be able to attract back the deposits which arise when the process of expansion starts with the making of loans and with the establishment of credit for customers. As long as it is able to attract back deposits, it will be able to expand. It will cease expanding at the point when either it cannot attract deposits from other institutions competitively, or when it loses cash. But the whole system hinges on the capacity of the central bank to initiate the transaction at the beginning of the line, and that is where the process of deposits expansion begins and ends.

Mr. JOHNSTON: Therefore, we would expect then that this increase will continue and there is nothing to prevent a further increase of \$100 million in the next few years?

Mr. MACINTOSH: Which figure do you mean?

Mr. JOHNSTON: December 1965. This process of increasing in the Bank of Canada deposits and notes will continue.

Mr. MACINTOSH: No, sir. We can go no further but the central bank can. The central bank's capacity to add to its assets is more or less unlimited, except that the central bank exists for the purpose of stabilizing the economy and does not act that way, as no central bank in the world would. The central bank attempts to gauge its policy to the legitimate requirements of the economy and that is all. But if you take this balance sheet to which you are referring at December 1965, it is quite impossible for the chartered banks to expand their deposits, given this balance sheet and given the holding of cash reserves constant by the central bank. It is absolutely and explicitly impossible. Incidentally, the same would be true of the near banking system, it also could not expand.

Mr. JOHNSTON: But if the central bank does proceed in the manner that it must have obviously proceeded in the past, then the expansion becomes possible.

Mr. MACINTOSH: Yes, if the central bank chooses to add to its assets, this can lead to an expansion. If you look at the second page—let us say a trust company—their cash expanded from \$41 million in 1960 to \$98 million in 1965. That is an increase of 139 per cent. If you ask me how this came about, all I can say is that it came about in exactly the same way. It did not come out of the air any more than it did in the case of the chartered banks. If you turn to the next page, the cash reserves of the *caisse* went up from \$168 million to \$283 million in that period. How come? Was it created out of nothing? No, it came through the same process of credit expansion, incidentally, with the larger rate of increase than in the case of the banks, for the reasons which the banks are very concerned about.

Mr. JOHNSTON: But if the central bank does make the increase of \$100 million, then the banks will be able to expand credit by making further loans? This is the process.

Mr. MACINTOSH: Yes; there must be some system in the economy obviously for expanding the amount of credit as the economy grows. If this were not the case, then the system would be ground down with deflation and a recession, if the money supply were not expanded by the actions of the central bank; that is what it is for.

Mr. JOHNSTON: And it starts here and works through the chartered banks.

Mr. MACINTOSH: It starts here, works through the chartered banks and, through them, through the whole financial system.

Mr. JOHNSTON: One other question then. In the brief quite a reference is made to the proposed reduction in cash reserve ratio. What effect would that have on the money supply?

Mr. MACINTOSH: In the first instance it probably would have none, because of the fact that the central bank would off-set its effect on the banking system. If you will look back to what happened in 1954, when the cash reserve ratio mechanism was changed, the same thing happened. As it happened, we were then entering a period of recession in 1954 to 1955. There was, in fact, a fair bit of expansion in the volume of credit and the money supply at that time. But, that was to counteract recession. Other things being equal, if the economy were to remain at its present rate of growth, the Bank of Canada would then attempt to fix the total dollar amount of cash reserves in such a way as to be consistent with the growth rate that it is attempting to achieve. Looking at the fact that the



cash reserve ratio will fall from 8 per cent to 6.6 per cent, the Bank of Canada can instantly off-set that, and would do so, with open market selling. It would do the reverse of the process that we have been talking about. Otherwise, if the cash reserve requirements of the banks fell from \$1.4 billion by shall we say, approximately  $\frac{1}{8}$  of that, which would be say \$150 million, the cash reserve requirements of the banks would go down. To put it another way: the amount of credit that could be established by the banks would go up if this figure were left unchanged. What would happen is that the central bank would go into open market selling operations, reduce its assets by \$150 million, and completely off-set the difference. So, the banks would end up with the same liabilities, the same earning assets of cash reserves which are smaller by \$150 million.

Mr. JOHNSTON: On the other hand, if the central bank fails to take the action you have spelled out, this would result in an increase in the—

Mr. MACINTOSH: Well, certainly. But then that amounts to assuming that the central bank does not know what it is doing; that they simply are going to, in an uncontrolled way, let the change in the act lead to hyper-inflation. Well they can do this now; they do not need a change in the act to do that. They can go out and buy \$1 billion in securities tomorrow if they like. But, you have to assume that the central banking system is being run by reasonable men, which, I am happy to say, is the case.

The CHAIRMAN: Have you completed your questioning at this stage, Mr. Johnston?

Mr. JOHNSTON: Yes.

(Translation)

The CHAIRMAN: Mr. Latulippe?

Mr. LATULIPPE: Thank you very much, Mr. Chairman. To begin with, I think the Committee should embark on the actual decennial revision of the Bank Act. It does seem to me that we are not quite clear on what we have been doing up to now and that we should now begin this examination. We can read here that "this Bill is the decennial revision of the Bank Act. The charters of the banks will expire under the present Act, as amended, not later than the 60th sitting day of Parliament after November 1966. Under the terms of this Bill the banks will be empowered to carry on business for a further ten years. The references below are references to the corresponding provisions of the present Act." I think that following the word business, in the Explanatory Note, we should add instead "up to April 30, 1974." This would retain the actual decennial period.

The CHAIRMAN: Would you have anything to say about that suggestion of Mr. Latulippe's?

(English)

Mr. PATON: Our preference is to retain the 10 years—10 years from the time of the revision to the next revision.

(Translation)

Mr. LATULIPPE: For ten years then, this would take us to 1974. So in this paragraph, instead of saying "another ten year period", we should indicate the year 1974. Does the Committee agree on that matter?

● (4.15 p.m.)

The CHAIRMAN: We are not discussing the Act clause by clause. We are here to question witnesses on the general principle of the Bill, and on connected matters. You can ask the witness how he feels about your proposal and it will be up to the members of this committee to decide if we should accept the suggestions or not. If you want to sit with us later as a witness, you could, of course make a statement on that. It might be better, at that point, to attempt to convince us, as members of the committee, that your particular ideas are the proper ideas in this instance.

But I have no objection, as Chairman if you want to put your idea to the witness. If you want to ask him for answers to your questions. We would of course ask the people here what are their feelings on the matter.

Mr. LATULIPPE: I think we should start off on a very clearly understood basis. When we start building, we should start with the foundations.

The CHAIRMAN: You can put your questions to the witnesses. I have absolutely no objection to that. But I have made that observation in order to assist you. I believe that you feel that we, as a committee, are now being called upon to vote on your ideas.

Mr. LATULIPPE: I think I understand the information. We are dealing here only with the brief. Still I believe it might have been proper to try to make the bill more perfect.

The CHAIRMAN: I assure you that the committee will take your ideas into consideration, but this will be done later.

Mr. LATULIPPE: Now Mr. Chairman, In clause 69 of this bill, could you tell us what is the internal reserve of the banks accumulated over the last 20 years. Such reserves not having been made public either to the shareholders or to the minister, what is the amount in the case of all banks, for this year 1965-66, and for 1964-65?

The CHAIRMAN: I am sorry, Mr. Latulippe to have to interrupt your line of questioning, but I wonder what does the Committee feel in this matter. Are we entitled to ask for things like that? Things that Parliament itself could not ask?

Mr. LAMBERT: On this matter, Mr. Latulippe is dealing here with the amount of hidden or internal reserves which were not communicated to the minister of finance. But Mr. Elderkin's testimony and Mr. Payton's testimony indicated that all this was controlled periodically on an annual basis. Banks must declare such a balance and state that these internal reserves are actually communicated to the minister of finance under the Act. I am not a witness in this instance, but Mr. Elderkin did give evidence. As a matter of fact, he tabled schedules related to these reserves. These must be part of the record of this committee.

(English)

The CHAIRMAN: Gentlemen, are there any reserves which you have not declared to the Minister of Finance?

Mr. PATON: No sir, there are no reserves not known to the Minister of Finance through the Inspector General.

(Translation)

Mr. LAMBERT: A little information. This is Schedule 14 which was tabled I believe, yesterday morning. I think Mr. Latulippe will find his information there. It has been given by Mr. Elderkin.

Mr. LATULIPPE: According to what we see here in the report and also to several briefs, some reserves have not been made public. That is why I was putting that question.

The CHAIRMAN: Public to who?

Mr. LATULIPPE: Declared to the Minister of National Revenue.

(English)

The CHAIRMAN: Would you confirm, or otherwise, whether there are any reserves which under the law do not have to be declared through you to the Minister of Finance?

Mr. ELDERKIN: There are no reserves which under the law do not have to be declared to the Minister of Finance. If you will look, Mr. Chairman, at exhibit No. 14 you will see on page 2 of that exhibit that at the end of the 1965 fiscal years the contingency reserve if fully used could have amounted to \$418.6 million. But there is a note showing it was only about 75 per cent filled.

(Translation)

The CHAIRMAN: Do you wish to continue Mr. Latulippe?

Mr. LATULIPPE: I will return to another point later, but I would have another question to put, on item 71(a) of the bill, I feel we should add another paragraph here, providing for a ceiling on the bank rate which is now 6 percent. Clause 71, as it happens, deals with the limitation on the dividends paid by the banks in respect of the paid up capital. This is, among other considerations, limited to 8 percent. But in this item there is no ceiling fixed with regard to the rate of interest. You could fix it at 8, 10, 12 or 15 percent, but at least you could provide for one.

Mr. LAVOIE: I have the impression, Mr. Latulippe, that you have not grasped the difference between the interest rates we charge on loans, and the dividends we pay. These are two completely different things. You speak for instance, of the interest rate on loans. In that regard the present ceiling is 6 per cent. A new form has been suggested in the Act. But if you are dealing with dividends, these are declared by each bank taking into account the profits made during the year. These are two different things.

Mr. LATULIPPE: I have reference here to interest on loans.

Mr. LAVOIE: This is something else altogether. Clause 71 deals with the matter of dividends, i.e. dividends paid to shareholders in chartered banks.

Mr. LATULIPPE: Then I think it must be under 72.

Mr. LAVOIE: This deals with primary and secondary reserves.

Mr. LATULIPPE: On that point; no interest rate is fixed by this bill.

Mr. LAVOIE: But what interest rate are you talking about, Mr. Latulippe. Interest rates on the loans we are going to make?



Mr. LATULIPPE: Interest on loans, yes.

Mr. LAVOIE: In that case, you should read Clause 91: Interest and Charges. There is a very simple formula proposed under paragraph 3. It provides for the maximum rate of interest or rate of discount per annum that the bank may charge on a loan or advance referred to in subsection (2), calculated on the basis of the market-yield on short term bonds of Canada.

Mr. LATULIPPE: But this does not mean that your rate is fixed. It might vary.

Mr. LAVOIE: Indeed it might. It will vary according to the formula proposed in these proposed amendments for the Bank Act.

Mr. LATULIPPE: Since the rate has always been fixed it would appear to be logical to begin with a fixed rate, whatever it may be. It would have to be fixed so that each citizen may know exactly where he stands.

Mr. LAVOIE: The present maximum rate is 6 per cent, but on the basis of the suggested formula—

Mr. LATULIPPE: But it is being removed entirely.

Mr. LAVOIE: Oh, no, we are not removing the ceiling completely. The point here is that we are putting a suggested formula forward under this Bill. I have just mentioned that formula.

Mr. LATULIPPE: But the rate of interest will not be fixed.

Mr. LAVOIE: It will be a maximum rate, there will always be a ceiling.

Mr. LATULIPPE: But what is the purpose of this? Why do you want to increase interest rates?

Mr. LAVOIE: I was reading the newspapers again this morning and I noted that in the Province of Quebec, the government had issued securities over a 20-year period at an interest rate of  $6\frac{3}{4}$  per cent. The interest rate is set by market demand.

Mr. LATULIPPE: I know all these things, but this bill is designed apparently only to increase the rate of interest, and since at the present time, there is a great deal of inflation, since the cost of living is very high, it does appear to me that if anybody is supposed to suffer deprivation it should not always be the same people. Those who have no money troubles. Those who play around with the people's money should be ready to forego this increase.

Mr. LAVOIE: This is not a matter of depriving oneself, it is a matter of market demand.

Mr. LATULIPPE: This does not suit everybody. This suits people who play the money market, it does not suit the purpose of the people who have to contend with the increased cost of living. But further, does the fact that you are now going to increase your interest rate, mean that you are going to increase your dividends, do you feel you are going to do that?

Mr. LAVOIE: I doubt if we are going to increase our dividends. Dividends are paid to shareholders, these are paid on the deposits calculated on a normal basis.

Mr. LATULIPPE: What dividends did you pay on shares in 1966?

Mr. LAVOIE: It varies from one bank to the other. There is not a single bank that pays the same rate of dividends as the others. It varies from bank to bank.

Mr. LATULIPPE: There must be an average.

Mr. LAVOIE: You mean the average yield of a share in a bank?

Mr. LATULIPPE: Yes.

Mr. LAVOIE: About 4 per cent.

Mr. LATULIPPE: So someone with a \$10 share—

Mr. LAVOIE: We are not dealing here with a par value, we are dealing with the market value. When I speak of 3 per cent or a little more, this figure is based on the market value of shares.

Mr. LATULIPPE: How much per share, 20 or 30 per cent, or something like that?

Mr. LAVOIE: Oh, no, it cannot. This is an average yield, between 3 and 3½ per cent.

Mr. LATULIPPE: As far as shares are concerned.

Mr. LAVOIE: That is a different matter entirely. The par value of those shares is \$10.00. Some shares are worth \$60, \$40 or \$70 perhaps. This depends on the market demand.

Mr. LATULIPPE: If you make a reasonable profit and if a share of \$10.00 reaches the value of \$60 or \$70 and if you declare a 20 or 30 per cent dividend on these shares, is it reasonable to increase the interest rate?

Mr. LAVOIE: I do not think I have understood your question properly.

Mr. LATULIPPE: If a \$10 share is now worth \$70?

Mr. LAVOIE: Yes, Mr. Latulippe?

Mr. LATULIPPE: And if the dividend paid in respect of that share has been 20 or 30, is it logical to increase the interest rate? Do you find that your profit is at a minimum, is that why you want to increase the interest rates?

Mr. LAVOIE: I have no figures here, but if you compare shall we say, profits made by chartered banks with profits made by other companies, I think it can be stated that the profits of the chartered banks are far from being excessive, on the contrary.

The CHAIRMAN: Are you through, Mr. Latulippe?

Mr. LATULIPPE: Yes.

*(English)*

Mr. PATON: If I might supplement what Mr. Lavoie said, we do have available for distribution to the Committee brief comments on the profitability of the Canadian banking industry, which might be of some help to you and I would be very pleased to have these circulated to the Committee.

The CHAIRMAN: I think that it would be useful and since it has been mentioned, I think it should be circulated and I invite a motion.

*(Translation)*

You may continue with your questions, Mr. Latulippe, as your time allotment is not expired.

Mr. LATULIPPE: Can anybody here tell me very clearly what difference there is between cash reserves and money?

Mr. LAVOIE: You mean the reserves we have in the Bank of Canada?

*(English)*

Mr. PATON: Have you finished the questioning, Mr. Latulippe.

Mr. LATULIPPE: No.

Mr. PATON: I am sorry.

The CHAIRMAN: Would you like to respond to this question of Mr. Latulippe.

Mr. PATON: The question, as I understand it was, what is the difference between cash reserves and money?

*(Translation)*

Mr. LATULIPPE: What is the cash reserve as compared to money?

*(English)*

Mr. PATON: The cash reserve we refer to Mr. Latulippe is the 8 per cent that we hold with the Bank of Canada, and that 8 per cent comprises a deposit with the Bank of Canada plus the Bank of Canada notes that the chartered banks hold in their branches right across the country, the two combined.

Mr. COLEMAN: Not plus, including.

Mr. PATON: Yes. The 8 per cent includes deposit with the Bank of Canada plus the notes that we have in our tills.

*(Translation)*

Mr. LATULIPPE: Do you mean to say it is the same thing?

Mr. LAVOIE: What Mr. Paton has just said is that the deposits made with the Bank of Canada by the chartered banks include the money of which you speak.

Mr. LATULIPPE: The bank notes. Why use two words here? Why do you make a distinction here in the same clause as if it were two different things?

Mr. LAVOIE: But it is not quite the same thing. It is included in the same clause but there are two parts of the same thing.

Mr. LATULIPPE: Could you give us a definition of Canadian money?

Mr. LAVOIE: Of Canadian money?

*(English)*

Mr. PATON: Could I suggest that this is something that Mr. MacIntosh might endeavour to clarify in answer to your question. Mr. MacIntosh could you, please?

Mr. MACINTOSH: The conventional definition of the supply of money in Canada is ordinarily taken to be total currency in circulation: that is bank notes, plus the Canadian deposits of the chartered banks; that is the money supply. It is a limited definition because it does not take account of further deposits of new banks, but the reserves are the portion of the liabilities of the Bank of Canada which are represented by the deposits of the chartered banks at the Central Bank. They are two different things. To put it another way, if you look at the balance sheet of the Bank of Canada, on its liability side it has two important items. One of these is currency, the note circulation. The total amount of currency issued by the Bank of Canada at November 2, was \$2,606 million. Of that sum, a portion was held by the chartered banks, because they find it necessary to have some cash in the tills for their ordinary purposes. The amount that was in the tills on that date was approximately \$420 million. The difference



between the total liabilities of the central bank in the form of notes of \$2,606, million and the amount of \$420 million which is in the cash of the chartered banks, in other words an amount of about \$2,200 million is the currency in active circulation held by the public, including all other new banking institutions. In addition to that \$2,200 million, which is held by the public in the form of bank notes, there are the further deposits of the chartered banks, which amount to approximately \$19 billion. These two items together are normally taken to be the money supply in the country.

*(Translation)*

Mr. GRÉGOIRE: I was just about to say that Mr. Latulippe's time has expired. He has had a little more than 20 minutes, even taking into consideration the other interventions which took place at that time, that is the answers given. I would suggest to Mr. Latulippe he should take these rather complicated matters into account and return to this item when his turn comes next time around.

Mr. LATULIPPE: May I put one other question? I do not find the answers very easy to understand.

Mr. LAVOIE: I will try to give you a very short and clear answer.

The CHAIRMAN: Mr. Lavoie, I must interrupt you also.

*(English)*

Mr. LAFLAMME: I would just like to say that Mr. Latulippe did not ask what the total currency in circulation was, tu as compris. He simply asked for a definition of money.

Mr. GRÉGOIRE: Moreover he did not ask about money supply, but what Mr. Latulippe meant by "La monnaie canadienne" was legal tender. That is what I want to mention, the difference, because he did not—

The CHAIRMAN: Have we unanimous consent to continue this discussion, if it is necessary to clarify this question.

Mr. GRÉGOIRE: It is a question of translation of words.

*(Translation)*

Mr. LAVOIE: What you want to know is what legal tender is? It is a whole of the liabilities of the Bank of Canada, including Bank of Canada notes and the deposits made at that bank.

Mr. LATULIPPE: It is scrip money, is it?

Mr. LAVOIE: Oh, no, no, no.

Mr. LATULIPPE: May I be allowed one other question or is my time up?

The CHAIRMAN: Perhaps Mr. Baribeau could explain further. Could you give us another definition of that?

*(English)*

Mr. BARIBEAU: The money supply is usually considered to be Bank of Canada notes and coins outside the chartered banks. The reserves of the chartered banks are not part of the money supply. And then you have the deposits of the public in the chartered banks. The public means, the general public and it

does not include the government or the deposits of the chartered banks in other chartered banks. That is the definition of money supply. These are the only two items entering the money supply.

Mr. MACINTOSH: Mr. Chairman, that is the identical definition to the one I gave.

The CHAIRMAN: My calling on Professor Baribeau was not intended as any reflection on the answer, but I thought it might help Mr. Latulippe in finding the answer in which he is interested, to this very useful question.

● (4.30 p.m.)

(Translation)

Mr. GRÉGOIRE: A question of information. Could we ask Mr. Baribeau to give us the French term with the English term, for instance, is "money supply" in English, "masse monétaire" in French?

The CHAIRMAN: That is a very interesting question. Would Mr. Baribeau please sit down there?

Mr. GRÉGOIRE: There are three or four terms that we should agree on. What you call "money supply" in English, is what we call "masse monétaire" in French?

Mr. BARIBEAU: Exactly. For certain purposes we have included deposits of the government in chartered banks, these will sometimes be included in the money supply, but in actual practice, for certain analyses of the money supply we would not include government deposits in chartered banks.

Mr. GRÉGOIRE: "Legal tender" in English is the same thing as "monnaie légale" in French?

Mr. BARIBEAU: Yes, under the Act.

Mr. GRÉGOIRE: And money supply includes both money supply and legal tender?

Mr. BARIBEAU: It includes deposits in chartered banks plus Bank of Canada notes in circulation and small coins, but not small coins and Bank of Canada notes held by chartered banks. These do not come under the definition of money supply.

(English)

The CHAIRMAN: I think that we have accomplished the end which the committee wished to follow permitting further time to Mr. Latulippe and I called upon Mr. Baribeau to assist in the quest of the translation, if I may put it that way, of terminology which may not appear to be the same in the two languages.

I want to make clear, I am not at this time inviting a general discussion of this very interesting topic. I am attempting to do two things. First of all as a gesture of courtesy to Mr. Latulippe the Committee wished to give him some extra time to have his answer completed, and secondly, I felt it might be useful for all concerned to have this answer to Mr. Grégoire's point, for which I thank him, on the question of the equivalent in the two languages of these useful terms, and unless there is some serious and well-founded objection, I think we are now in a position to begin our second round of questioning. You will recall our discussion this morning. We are going to try to follow the suggestion of the steering committee and go over the brief of the Canadian Banker's Association

section by section. May I suggest to the committee that they consider the preamble along with Section headed "Interest Rate Ceiling". Therefore the first section we will deal will extend up to the top of page six, and ends with the second paragraph. The list I have in this regard, which was actually given to me for the second round, before this type of discussion was suggested by the steering committee, is as follows: Mr. Monteith, Mr. Clermont, Mr. Lambert, Mr. Fulton and Mr. Lind. Mr. Flemming has asked if he could have a period of questioning when he comes back—he had to take an earlier train than he thought he would—and as a courtesy, I suggest we afford him that opportunity. If those whose names I have mentioned do not feel that, because of the type of procedure we are following, they like to proceed in that order, I am prepared to modify it.

Mr. MONTEITH: As I understand it, Mr. Chairman we are more or less going to dispose of the interest rates part of this at this stage. We can always come back to it of course.

The CHAIRMAN: I suggest that, to save time, we also include the preamble to the brief.

Mr. MONTEITH: On page 3, there is a recommendation or a comment by the Porter Commission. Section (b) reads:

- (b) More specifically, the ceiling stands in the way of flexible lending by the banks in that it frequently prevents them from making loans on which higher rates must be charged to cover administrative costs and risks.

Now, I understand the Canadian Bankers' Association agrees with this comment. I can understand that there should be higher interest rates on greater risks. I am just wondering what type of administrative cost might be increased because of this type of loan. Might it be examination of a type of asset that is given as collateral, or this sort of thing. Is this what you visualize. Can you give me any example of how the administrative cost might be greater because of a higher risk.

Mr. PATON: I think I will try, Mr. Monteith. Credit supervision in any bank is a major cost to the bank. Wherever there is a higher risk to the loan there is also the necessity for closer, more continued, more repetitive supervision. For example, in business loan, where the risk is somewhat extended or greater than in other cases, monthly figures might be received as to the inventory position, or general security position, say the receivables position; in other words, the attention to that loan, by virtue of information supplied by the customer to the bank is considerably greater than in other instances where the credit risk is considerably better. That is the major administrative cost and indeed it encompasses the over-all bank. It starts from the manager of the branch, who spends more of his time on a loan that requires closer supervision, than he does on another account where the statement position of the company warrants a less attentive approach to the operations.

Mr. MONTEITH: The way in which this word "administrative" is used does not apply to the actual administration of the account for service charge purposes or this sort of thing?

Mr. PATON: No sir, this would enable us to take on higher risk lending taking into consideration additional time that would be required at the branch level, at the divisional level and in due course at the—



Mr. MONTEITH: Mr. Chairman, I do not know whether we are going to have the different banks before us individually.

The CHAIRMAN: Some have already signified. I can inform the Committee that the Royal Bank of Canada, the Montreal Bank and the Mercantile Bank of Canada have asked to appear before us. If it is the intention and the desire of the Committee that others be invited, I am sure—

Mr. MONTEITH: I meant in the personal loan field. During the study in 1954, the Canadian Bank of Commerce was primarily the only bank which was in this business at that time. I suppose a general question would be in order on the matter. For instance, I understand the effective rate on the personal loans, if my memory is correct, at that time was either 10.48 or 10.84 per cent. If the interest ceiling is raised from 6 per cent to an effective rate of 7 per cent or  $7\frac{1}{4}$  per cent as the case may be; now it is 7, would this mean that the effective rate on personal loans would be considerably higher than the 10.48 per cent at that time. It was based on 6 per cent.

Mr. PATON: No, sir, that would definitely not be the case.

Mr. MONTEITH: Any personal loans would well then remain at the same basis of interest charges as they are now?

Mr. PATON: I would say, could well, instead of would well. I cannot say, would well, because this is again a question for each individual bank to make its decision as to how its mix of assets would be affected, but no automatic increase would be attributable to these types of loans simply because the interest rate would be free. Indeed if the interest rate was increased and there were additional funds available for this type of lending, it is conceivable that with a larger pool such rates might go the other way. I would say that a fluctuation would be there, but not necessarily upwards, and it might well stay at the same level.

Mr. MONTEITH: My recollection is, as I recall the evidence of that time, that the legal—I do not suppose it is appropriate to say this, with the Bank of Commerce people not in the room—to the effect that the Bank of Commerce did have the advice of solicitors at that time that they were acting quite within the terms of the Bank Act in making this type of loan with an effective rate of interest of 10.48 per cent. Now, as The Canadian Bankers' Association, I do not know if they gave evidence at that stage in 1954 or not on this particular point, but I am wondering if you as the Canadian Bankers' Association have had any legal advice as to this procedure on adding because I know other banks have gone into it since then, and loaning at other than a ceiling of 6 per cent.

Mr. PATON: The association as such did not need to obtain legal advice on it, but I think I would speak quite correctly if I said that each bank now in this form of financing, and I think that includes all eight, individually received advice from counsel that the manner in which they were proceeding to lend under the personal consumer loan financial plan was quite within the ambit of the act.

The CHAIRMAN: Mr. Paton, do you have someone from the Bank of Commerce with your delegation?

Mr. PATON: Yes, I was going to suggest that there is in the audience someone from the Bank of Commerce and I would be very pleased to call him up.

The CHAIRMAN: It would not be otherwise than appropriate. I would like to invite them to come forward. They may confer or respond directly to Mr. Monteith's question; I think it is quite in order.

Mr. PATON: Mr. Sharwood, would you care to come up and join us? Mr. Sharwood, is Deputy Chief General Manager of the Canadian Imperial Bank of Commerce.

Mr. MONTEITH: Well, I think I have almost finished my questioning, Mr. Chairman, at this point, but I suppose I could put a direct question to Mr. Sharwood. I do not recall his being before us in 1954; however, since the evidence at that time was I think to the effect that the legal advisers of the Canadian Bank of Commerce as it was then known, had advised that it was quite within the terms of the Bank Act to handle these small loans in the manner in which they were being handled, even though the effective rate was 10.48 per cent.

Mr. J. R. SHARWOOD (*Deputy General Manager of the Canadian Imperial Bank of Commerce*): That is correct.

Mr. MONTEITH: Your advice to this effect under the present Bank Act would still be the same?

Mr. SHARWOOD: That is correct.

Mr. MONTEITH: Maybe I could ask Mr. Sharwood this question directly. He has undoubtedly been over the terms of the revision of the Bank Act. Is there any clarification in the new legislation concerning this particular point, as to what interest may be charged?

Mr. SHARWOOD: I think that if the ceiling remains, and is not lifted entirely, Mr. Monteith, and if the parts of the act which suggest the formula at present under Section 91 remain and were not removed entirely, there would be no change in the way in which our bank at least would consider that they would operate their personal loan systems. I cannot speak for the other banks of course.

The CHAIRMAN: Mr. Elderkin, do you want to supplement that in any way?

Mr. ELDERKIN: No change in the present act, Mr. Chairman, as far as that particular section is concerned.

The CHAIRMAN: Mr. Monteith, are you prepared to yield for a supplementary of Mr. Gilbert?

Mr. MONTEITH: Yes.

Mr. GILBERT: Mr. Chairman, I wonder if the witness could tell us what authority under the act gives him the right to charge this additional interest? What is the section?

Mr. SHARWOOD: Mr. Monteith, may I say something which I hope may clarify this point? You refer to the effective rate of interest? This is not; it is the effective cost to the customer, it is not the effective rate of interest. The interest rate is 6 per cent; the other charges make up the difference between 6 per cent rate and the effective cost to the customer which in the Canadian banks range from 9½ per cent to 11.

Mr. MONTEITH: In other words it is insurance or whatever you have, this type of finance company, they run up to 20 odd per cent on occasion.

Mr. SHARWOOD: That is correct.

Mr. GILBERT: Mr. Chairman, I would just like to go back and ask what section of the act?

Mr. PATON: Section 93(3) is the section that provides the authority to which you refer.

Mr. SHARWOOD: I think it would be appropriate to say, Mr. Chairman, that there is a difference in the methods of operation of our bank's personal loan scheme and those of the other banks. Our bank's legal advisers base their opinion on the operation of our system on Section 91 where it says that the bank shall not—I have not the section in front of me, but they shall not levy a rate of interest or discount, and we discount the original note at 6 per cent. I do not feel qualified to go into much detail about the operations of the other banks, perhaps Mr. Coleman would, but as I understand it, they rely on the contractual agreement of the bank to levy a service charge, and there is some difference in the operations between the personal loans scheme of our bank, which was fully set out in the previous hearings, and those of the other banks.

The CHAIRMAN: Which previous hearings are you referring to?

Mr. SHARWOOD: In 1954.

The CHAIRMAN: Most of us were not here either.

Mr. MONTEITH: Mr. Chairman, as you have indicated the interest rate may be increased, to cover greater risks. I can understand that argument, but I am thinking of the protection of the small borrower. It has also been intimated I think that he is not going to suffer; that the higher interest rate will probably apply in some other way. First of all if this interest rate is raised, I can understand on the greater risk that it should be applied, but what protection is there going to be for a person who has Dominion of Canada bonds as collateral; what is going to be his protection so that he does not pay 7 per cent instead of 6?

Mr. PATON: Basically, the answer, Mr. Monteith, would be competition between lenders for money. A man with Dominion of Canada bonds would be assured that he would be getting the best available rate of interest there is in the country because the security is undoubted, the administrative costs are relatively negligible in relation to others, and the man who has security of that nature would receive the best possible rate.

Mr. MONTEITH: Well, we will take a bigger company who has a million dollar line of credit with you; how is the increased ceiling going to affect his borrowings?

Mr. PATON: It is difficult to forecast exactly what would happen to interest rates generally but present conditions when money is very tight and loan demand is very high, the necessity of acquiring deposits to meet this demand will be basically the prime concern of the banks. Having reached that objective as we would certainly hope we could, it would then enable us to take on the loan applications we have; it would intensify the competition between lenders in this area, and would tend to keep the rate of interest to the man with the million dollar line of credit at the lowest possible figure. I would be quite incorrect to say that there is absolutely no possibility of his paying more than 6 per cent, but in view of the open competitiveness of the new situation, and the ability to look after the requirements, would undoubtedly over a very reasonable period—



Mr. MONTEITH: The old law of supply and demand.

Mr. PATON: Exactly so.

Mr. MONTEITH: I had a supplementary in my mind, but I was so busy listening to your answer that I have forgotten it. Sorry, Mr. Chairman, I will come back; you might as well carry on.

The CHAIRMAN: Thank you.

Mr. LAMBERT: In this region, is this going to be still on the interest rate?

The CHAIRMAN: We are still on it. We are following a suggestion of the steering committee which is that we limit this round of questioning until we exhaust ourselves—if that is the right word—on this section of the brief which seems to cover pages 1 to 6.

● (5.00 p.m.)

(Translation)

The CHAIRMAN: I would now recognize Mr. Clermont. You will put questions on interest rates and related questions.

Mr. CLERMONT: Must my questions be directed merely to the matter of the rate of interest ceiling? Is that it?

The CHAIRMAN: Your question must relate to that subject.

Mr. CLERMONT: To a question put by Mr. Latulippe to Mr. Lavoie, Mr. Lavoie answered that if Parliament were to accept bill C-222 there would still be an interest rate ceiling. Would Mr. Lavoie give us more information on this?

Mr. LAVOIE: To answer your question, Mr. Clermont, it is clearly mentioned in the Act that this interest rate will remain until the yield of the Dominion of Canada bonds fall under  $4\frac{1}{2}$  per cent.

Mr. CLERMONT: I believe you used the word "always".

Mr. LAVOIE: I might have said so, but I should not have said so.

Mr. CLERMONT: Mr. Chairman, I put a question to Mr. Lavoie myself last Tuesday in respect of the balances which the banks should require the customers to keep in order to balance their accounts, he answered that banking operations are such that it is no more expensive for the bank to lend 1 million dollars than to lend \$1,000. Does Mr. Lavoie not feel that a firm can have credit enough to borrow 1 million dollars from the bank, could go on to the money market instead of going to a chartered bank, could they not leave this area for consumer loans?

Mr. LAVOIE: Mr. Clermont, when I last mentioned this question to which you have just referred, I was simply dealing with the cost of entry. Take, for instance, a bank employee who enters things in the books, whether he is entering a million dollars or a thousand dollars, it is pretty much the same type of work, it is a matter of operating costs in themselves. That was the purpose of my reference.

Mr. CLERMONT: Do you take credit risks into consideration at this point, because the fact that you are granting a loan of one million dollars or one of 1,000 dollars, does not really mean that a loan of 1 million dollars would be

repaid more easily than a thousand dollar loan. There is a greater credit risk with regard to a million dollar loan, is there not?

Mr. LAVOIE: Well, when you are lending 1 million dollars, you really require security.

Mr. CLERMONT: Yes.

Mr. LAVOIE: But if you are lending 1,000 dollars, you sometime do without security.

Mr. CLERMONT: It is clear that you need 1,000 dollars in order to guarantee the payment of 1,000 dollars—

Mr. LAVOIE: In the banking system, there is a great deal of competition and I am convinced that if a customer goes to a chartered bank to obtain \$1,000 this is merely an ordinary banking risk. If the customer can pay back his loan as required, there will be no difficulty in granting it. If he had any trouble with one bank, he would certainly be able to obtain a loan from the other bank, because there is a great deal of competition.

Mr. CLERMONT: You say there is great deal of competition in the banking system, but if we refer to the report of the Porter Commission there seems to be a feeling that there is not enough competition at the present time. It seems to me that the interest rate for the banks seems to be an item of capital interest insofar as the proposed amendments to this Act are concerned.

Mr. LAVOIE: I really believe there is a great deal of competition between banks.

Mr. CLERMONT: Is there not some measure of agreement between yourselves, do you not feel that you are not attempting to steal customers from one to another?

Mr. LAVOIE: I could answer this in this way. In the case where you have three or four banks, I am convinced that it is the most active of the bank managers who will obtain the bigger part of the business.

Mr. CLERMONT: Speaking of competition, when the administrators of the proposed Bank of Western Canada came before this Committee, Mr. Coyne, I believe, said that as far as they were concerned,—Mr. Chairman, this does not refer to the field of interest rate, but this is a related matter—they would have no compunction in finding their staff in the present banks. A remark along the same line was made by one of the provisional administrators of the proposed Bank of British Columbia. At the present time, is there not the same measure of agreement so that there would no solicitation of staff from one bank to the other? Yet for other financial analysts this proposed removal of the bank rate is not really all that important. What is important is the increase of competition among the banks or greater diversification of the reserves accumulated against possible losses on loans, or even decrease in the buying into our banks by large foreign banks or financial concerns.

Two or three times you told me that there is considerable competition between banks. Do you really think there is that much competition, Mr. Lavoie?

Mr. LAVOIE: There is no restriction of that kind, nothing prevents an employee of a bank from resigning and taking employment in another bank. There is nothing to prevent that. There is no agreement among chartered banks concerning their staff, as far as I am concerned. There is no such thing. Bank

employees are perfectly free to work for one bank or another. This, in fact, is quite frequently the case, in particular among female employees working in a branch, who might prefer working closer to their home in another branch, they will not hesitate at all to resign and to accept employment with another branch. There is no such agreement between banks.

Mr. CLERMONT: You spoke of competition between the banks, and the members of your association. If a new customer comes to one of your branches, will this branch ask for financial information about him from another branch?

Mr. LAVOIE: Yes, this is common. There is exchange of financial information.

Mr. CLERMONT: But this information is confidential?

Mr. LAVOIE: Yes, this is confidential information.

Mr. CLERMONT: If I must deal with interest rates alone I think I will pass my turn.

*(English)*

Mr. LAMBERT: Yes, there are three sectors in this general area which I would like to talk about. First of all I understand that in reply to Mr. More this morning, Mr. Paton in, shall we say, looking at the crystal ball, said that on the basis of present rates of interest it might conceivably be that during the lifetime of this particular act the effective 7 per cent ceiling would apply. In other words, it is quite conceivable that the rate on short-term government obligations would not decline below  $4\frac{1}{2}$  per cent in order to spring the unlimited ceiling on interest rates. Am I correct?

Mr. PATON: That is correct.

Mr. LAMBERT: Now, secondly, because of the exceptions to the ceiling on interest included the proposed clause 91, and because you in your brief suggest that it would be preferable to remove the ceiling entirely, could you perhaps make an estimation of the possible business that you might anticipate in shall we say the unlimited interest rate sections as against those in which there is a 7 per cent rate? After all there are some rather wide provisions, exceptional provisions in 91; for instance, there is no limitation on interest rates on residential premises, on those mortgages; nothing under the National Housing Act. There are none with regard to maybe bridge loans. I would suggest to you that it would be very easy to devise a way to handle advances to contractors on projects who will themselves be the projected mortgagors in the initial instance, and they will make general assignments of the proceeds of these mortgages and there are a number of other provisions.

Now, how much freedom do you anticipate that these exceptions under 91 will give you in regard to the totality of your business?

Mr. PATON: There is a ceiling on mortgages, Mr. Lambert.

Mr. LAMBERT: Yes, but not imposed by this act.

Mr. PATON: That is correct.

Mr. LAMBERT: If the Governor in Council and the board of directors of Central Mortgage and Housing Corporation in their wisdom were to raise the interest rate on N.H.A. mortgages to  $7\frac{3}{4}$  per cent, you could operate over 7 per cent?

Mr. PATON: Perhaps I may interject that we have seen little evidence of this wisdom in connection with other rates of interest on government guaranteed loans



that we are presently operating under; so I do not anticipate that there will be any substantial change in their approach. No, the question you pose is a good one. A short but definite answer would be that there will be a definite corporate responsibility of the chartered banks to be good corporate citizens, and we like to think that our record for the last 150 years would indicate that we are quite capable of doing so. We are essentially commercial banks pledged to the development of Canada's industry, commerce and industry. I see no possibility of our entering into these higher interest vehicles to the detriment of looking after our normal business loans.

The statistics will indicate the extent of these latter loans. This will be an individual problem for each bank to decide under the new regulations, as to which way they will go; but there will not be, and I think I can speak very definitely on behalf of all of them, there will not be a sudden divergence of present loans financing the primary producers, the manufacturers, the secondary industries, the primary resource industries to the kind of loan yielding a greater return on funds by investing in the mortgage field or bridge financing as you suggest. Now this is not to say that we will not bend our best efforts to finance in this area, too, as they are an essential part of the whole economy of the country. It would be well nigh impossible, I think, to try to put any percentage, I think that was really the question. What change would there be perhaps in the type of loans the charter banks would engage in? Well,—

Mr. LAMBERT: Well, Mr. Paton, I must apologize if there was any implication that there would be a motivation or improper motivation by the banks. No, what I am concerned about is, on the mix of your loan portfolios as they are today, I am sure that somewhere along the line the banks have put a yardstick of their operations on the basis of the new act to determine their attitude whether conditions will be liveable, really liveable, under the new act.

I can readily imagine that the economic advisers and those who would be advising the board of directors of any bank and of your own research people would say, well, on the basis of the type of general business we are doing today, perhaps 35 per cent of our business will now be freed of interest charge limitations; and therefore, if we are allowed to go up to one per cent more with a balance, this becomes quite liveable. This is what I am trying to get at, or if these exceptions, say in subsections 6 to 91, would represent only 5 per cent of your business, you say well thanks for nothing.

The CHAIRMAN: Are we coming to that, Mr. Paton?

Mr. PATON: I will make a brief comment on it and perhaps ask my colleagues here to add to it, because once again each bank is operating on its own particular problem and undoubtedly all of us have been taking a very hard look at what the potential situation would be on two counts: one, if the ceiling was completely removed as of January 1; and two, if it were a two stage operation. For my own bank we have not endeavoured to put a yardstick on how much business we would direct into these new fields. We realise that we have our depositors to consider. We would have to take a look at their picture in so far as the interest rates we are quoting them. Also we have a long standing connection with companies and businesses throughout the whole process of banking, many of whom would not come under the new sections. Their requirements might well increase as the economy develops. We would be under strong compulsion, naturally, to take care of their increased requirements. We do feel that ability to

compete, is needed and if all rates were freed entirely, we would have no inhibition in concerning ourselves with just how much we would have for each specific type of lending because the simple fact would be that the interest price would dictate just how far we could get into an area of, perhaps conventional mortgage lending which is a long-term area. Bridge financing is a temporary or short-term area, and in many cases we would be able to provide the ultimate mortgage financing that this bridge financing falls into. We would have to be very conscious that the relationship of our assets in the form of these loans would still permit us to look after the requirements of the calls on our deposits so that at all times we would be in a position to meet these calls.

I do not think, speaking for my own bank, and perhaps Mr. Coleman will supplement my remarks, I could give you an approximate figure that we are tentatively looking at that might well be the diversified in these new areas.

Mr. COLEMAN: Mr. Lambert, I would find it impossible to give you a definite figure but I would say that most of the exceptions in 91(6) relate to loans which would be secured by mortgages. Now this narrows the field down: mortgages, bridge financing and the purchases of securities of corporations. This does not open a wide field. I would say that the banks in mortgage lending will have to think of several things. But as you know, banks who have got into trouble over the years have been banks that have lent on a long-term basis from short-term funds. I think before the banks would be in a position to look for mortgage loans exclusively they would have to think very carefully: what is the position on the other side. If we are going to lend long here we are going to have to borrow long. It would depend on the funds we could attract on a long-term basis. If you are wondering, is the small borrower going to suffer, you may not be but if you are—I would say no. I think it is an interesting statistic that over two million Canadians, one out of every six adults, have personal loans from chartered banks today. One third of automobile financing in Canada is now done through chartered banks. I do not think there would be any inclination or desire for the chartered banks to do anything but increase the business in these areas if they have the funds to do so. So I do not think the other sectors would suffer.

Mr. LAMBERT: I am afraid that somehow or other the wrong inference is being drawn from my question. It is really based on the fact that your brief says you would like to place emphasis on competition and that you feel this two-stage operation, which is partly controlled and partly de-controlled, does not give you the ideal competitive quality that you would like. In arriving at an assessment of your position I naturally say, well, all right, within the act the interest on part of your business is going to be controlled, part is to be de-controlled. Now if the de-controlled portion is only 5 or 10 per cent on potential, then perhaps the act is merely tossing some crumbs to you; whereas, if on the other hand, you feel that on the present mix of loan business you are getting 60 per cent de-control, well then we may say, well, but your complaint of lack of competition or competitiveness is not nearly as strong as it might appear from your brief.

Mr. COLEMAN: Mr. Lambert, my judgment is that the additional business we would take on as a result of these exceptions would not be relatively substantial.

Mr. LAMBERT: Good. You said something about it being more or less all in the long-term field but I would have thought that under 91(6)(b)—if the



Chairman will allow me to make particular reference to it—that the bridge loans—

Mr. COLEMAN: Those are short-term loans.

Mr. LAMBERT: Yes. They are to cover assignments. If they are based on assignment of mortgage funds they are mortgage funds from any source, N.H.A., and other conventional mortgage institutions. The contractor who is putting up two houses, the contractor who is putting up 100 houses or even 500 houses in a year could be accommodated under this particular subsection?

Mr. COLEMAN: That is right, and the loans would be related directly to the funds coming eventually from the mortgage lender.

Mr. LAMBERT: Yes, but not of your particular bank.

Mr. COLEMAN: Not necessarily.

Mr. LAMBERT: No. As a matter of fact, it might be more outside the banking field.

Mr. COLEMAN: The reference in here said by another lender.

Mr. LAMBERT: That is all I had to say, Mr. Chairman.

The CHAIRMAN: I will now recognize Mr. Fulton. You understand, Mr. Fulton, that—

Mr. FULTON: I understand the decision is that we now go through the bankers' association submission, section by section. We are on the interest rates.

The CHAIRMAN: And obviously related questions, of course.

Mr. FULTON: Yes.

The CHAIRMAN: If you prefer to withhold your questioning at this point because of the new arrangement, well that is certainly acceptable. Otherwise, of course, I would have to give you the floor at this time.

Mr. FULTON: The only one amongst the questions I have down here that I think is related in this matter of the extent of mortgage lending. Perhaps I could ask a question or two about that.

The CHAIRMAN: It seems we are being inconsistent here. I think there is a separate section following immediately after the one on interest rates headed "Mortgage Lending".

Mr. FULTON: Well, perhaps I should defer my questions until later.

The CHAIRMAN: I am suggesting this merely so we are consistent with the procedure we discussed this morning. If you have no questions specifically related to interest rates, I am prepared to give the floor to Mr. Lind. You will probably have another turn at this as well, of course.

Mr. FULTON: Yes, I think I should try and follow up the agreement of this morning and defer my questions.

Mr. LIND: I will be very brief on the interest rates. I would like to go into the consumer loan end of it. I know they say the actual interest rate at the present time is 6 per cent charged by the average bank. But I would like to know the procedure followed in that. My understanding is they issue a note and then apply the note to the loan or deposit the loan in the bank. It seems kind of an intricate procedure and the customer signs an agreement to attach the service charges to the cost of the loan. Would you explain all that, Mr. Paton?



Mr. PATON: I will do my best, Mr. Lind. We did have one of our people with us who was pretty expert in this area. Unfortunately, he had to return to Toronto this afternoon and is not available.

The CHAIRMAN: Perhaps he knew Mr. Lind was going to ask this question.

Mr. PATON: I do not think so. I had the impression he was very much perturbed that he had to leave.

You could defer it until he returns or I could perhaps give you my own somewhat halting description of what I am aware goes on. Some of my colleagues may correct me or add to my remarks.

The CHAIRMAN: May I suggest that you attempt to deal with the question so Mr. Lind will have some information and if necessary next week the person to whom you referred can supplement or correct your answer.

Mr. PATON: I think in general it would be fair to say the majority of banks handle a personal loan, a consumer finance loan—that is the area I am in—on the basis that the customer goes to the bank manager and applies for a personal loan. He signs a note. Concurrently with the signing of that note he is advised exactly what he is paying in the form of interest and service charge, which is all embodied in the note. I may be out on details. This note can be repayable and is repayable normally on a monthly basis. It may stretch for 12 months, 18 months, 24 months. I think there is a general ceiling around 36 months. The amount of his monthly payment is advised him and also shown on this note. Every month he makes his payment and that is deducted from the principal amount of the note. A direct reduction is made on the note. Now, I am speaking of the majority of the banks. I might get Mr. Sharwood to come up here and he would supplement the rudiments or I should say the manner in which a consumer finance loan is put on the books of his bank and how the repayments are recorded.

The CHAIRMAN: Mr. Sharwood, would you like to come up here and supplement Mr. Paton's reply?

Mr. PATON: If there are other banks that have different systems they should be given an opportunity to supplement the reply as well, but my understanding generally is that it is the Commerce Imperial versus the rest.

Mr. LIND: Now, suppose the customer—

The CHAIRMAN: That was very gracious of you, Mr. Paton.

Mr. LIND: Suppose the customer has come into more fortunate circumstances, and is in a position to pay this consumer loan off at the end of the sixth payment instead of letting it go on to the twenty-third payment, what does he pay back to the bank?

Mr. PATON: He has a privilege, subject to a certain penalty, and I cannot give you that figure. Mr. Dickson when he returns with us will be able to do so; but my understanding, is that he would be enabled to pay off the full outstanding balance after the expiry of a certain time, at perhaps some penalty but nothing related to the total cost of the funds were he to meet the contract as it matures.

Mr. LIND: In other words, there is not any formula for this worked out?

Mr. COLEMAN: He would get a rebate on the interest which he was slated to pay. And, as Mr. Paton said, there would be a penalty for earlier payment. But he

would get a rebate; he would not pay interest for the full twenty-four months, if that is what you mean.

Mr. LIND: Yes, I know. But what I am coming to is the ratio. You will retain something for putting this business on the books.

Mr. COLEMAN: That is right.

Mr. LIND: Now, how much penalty does he pay? This is what I want to know.

Mr. COLEMAN: Mr. Lind, I cannot tell you, but there certainly is a definite formula. The same rules apply to all borrowers in each bank. There is a penalty in that he would not get his full interest rebate back, as far as I understand it. But I am not absolutely sure about that.

The CHAIRMAN: Mr. Lind, perhaps you might reserve that aspect of the question for Mr. Dickson's return. I would have thought that with all the banks here they would use this opportunity to promote their particular personal loan plan. I am surprised that they are not vying with one another to put forward the favourable features of this personal loan plan. However—

Mr. LIND: We are staying, Mr. Chairman, wholly within the interest rates here pretty well.

The CHAIRMAN: And then, obviously related matters?

Mr. LIND: Well, then, on the related matter in this regard I would like to ask one question. Is there an exchange of credit information between various banks on customers who are borrowing in the consumer field.

The CHAIRMAN: The consumer field?

Mr. LIND: Yes.

Mr. PATON: An exchange of credit information between banks regarding an individual borrower who comes in for a consumer loan.

Mr. LIND: Well, I know it exists in other loans, but I would like to know if there is in the consumer field.

Mr. PATON: Perhaps I might just enlarge a little on that, Mr. Lind. There is a very strong confidential relationship, of which you are well aware, between bank and customer. The banks do exchange confidential information on any of the borrowing customers, on receipt of a request from another bank. But this type of information is not detailed statistical statement information of the individual customer, unless that customer authorizes the disclosure of such information to an inquiring customer. As you well know, this happens quite frequently where certain corporations are looking for credit facilities from a supplier. They authorize the supplier to approach their bank, and in turn get information from the bank of the account of the recipient of the goods. This is on a very confidential and limited basis, unless specifically authorized by the customer saying it is quite in order to furnish so-and-so with details of my statement of information which you have on your file. In so far as consumer financing individuals are concerned my answer to that would be no, that there is not general exchange of information. If there is knowledge that an individual has a connection with the bank, and he advises the banker that he has, there would be every opportunity, and probably the opportunity would be taken advantage of, to check with the bank.

Mr. LIND: Suppose I went to the Bank of Commerce, which I have never done any business with, for a consumer loan—

The CHAIRMAN: Here is your chance, Mr. Sharwood.

Mr. LIND: —do you mean to tell me that there would not be credit information, if he phoned up the Bank of Toronto and inquired through your local office on my position, if I inquired on this.

Mr. PATON: Oh, yes. If he was being approached for information; as I said earlier, the information would be on a general basis unless you had already authorized—when you talk about the bank of Toronto, you date both you and me—the Toronto-Dominion Bank. He would have phoned us, you would have already talked to him about this loan, and you would know that he would be talking to us for a report on our experience with you as a customer. But unless you gave us authority to disclose the statement of information we had on you personally, and we might well have, if you had been a customer of ours, we would not disclose that.

Mr. LIND: If this was the first consumer loan I was going to take, how would you assess the credit risk?

Mr. PATON: My reply to you might not qualify me to be a manager of one of our branches; I have some colleagues here who will be reporting back to Toronto.

The CHAIRMAN: You do not have to be qualified as a branch manager, you are now general manager.

Mr. PATON: Nothing is fixed in this business. Perhaps Mr. Coleman would say something.

Mr. COLEMAN: Having been a branch manager not too long ago, let us assume you came into me and you wanted to consume a loan. I would say “Mr. Lind”—I would first look to see if you have any borrowing record, and you have not—“have you borrowed anywhere before, from any other bank”? What would your answer be, ‘no’?

Mr. LIND: No, I do not know—

Mr. COLEMAN: Would it be “no”?

It would be yes. I would say, what bank and you would tell me. Then I would say, well I will have to check your record at that bank. I might also decide to check with the retail credit bureau—there are bureaux in each community of any size—If I was not quite satisfied with the way you answered me. I might be satisfied to give you the loan. So, the answer to your question is, unless you have an established record at a branch, checking is done. You could not make a loan otherwise.

Mr. LIND: I will pass.

The CHAIRMAN: Next I will call on Mr. Gilbert.

Mr. GILBERT: Mr. Chairman, the first thing is a request. We had filed with us the classification of loans by the banks. I would like to ask the Canadian Bankers' Association if they would give us the effective interest rates, effective in the sense that it includes the interest and the service charges with regard to the different classifications, the high and the low of each classification?

The CHAIRMAN: What are the classifications to which you are referring?



Mr. GILBERT: They are set forth in the exhibit. The first is the government and other public services and there is a breakdown of that. The second is the investment dealers and brokers. The third is personal and the fourth is agricultural, industrial and commercial. What I want to know is the range of the low and the high effective interest rates for those classifications.

The CHAIRMAN: Do you have that information readily available at this time? Is there a problem here?

Mr. PATON: No. The form from which you quote covers the full loans of all chartered banks, every division of loan. The effective interest rate under normal times in all these loans would be at different rates. At the present time the minimum and maximum we have, in connection with the ordinary loan is 6 per cent.

Mr. GILBERT: I am not talking about the 6 per cent. I am talking about the effective interest rate which includes two items. It includes the interest under section 91; it includes the charges under section 93 (3). In other words the total cost of the loan as I understand is the effective interest rate. I just want the range, the low and the high, say for the past five years with regard to these different classifications.

Mr. PATON: Such information would be well nigh impossible, I think, to provide. The information on the personal lending—that one specific area—is available. We can supply you with certain statistics from each bank, in fact, we do have them ready, showing the total loan cost in the consumer finance field; the components of the total loan cost broken down into interest or discounts, service or administration charge. It is not expressed as an interest rate of the cost of the funds. It is shown in dollar totals. The sample taken is for a personal instalment loan or advance on a principal amount of \$1,000 repayable in equal monthly instalments. This information is available here and we would be very glad to supply it.

Mr. GRÉGOIRE: May I ask just a supplementary question.

The CHAIRMAN: If Mr. Gilbert will yield.

Mr. GILBERT: Yes.

Mr. GRÉGOIRE: Is it for each bank? Will we know what is the real interest or the real cost? Suppose I buy a car and I want to have it financed by a bank. Will all the banks have included in the interest their real costs?

Mr. PATON: There are eight sheets there covering each bank's figures but not designated by banks. I think it is bank A, B, C, D, and E, etc.

Mr. GRÉGOIRE: If I am interested in buying a car I will not know. I will have to find out who is A, who is B and so on. I am asking, Mr. Chairman, because I am changing my car and I would like to know.

Mr. PATON: You would, perhaps, have to go to eight banks individually.

The CHAIRMAN: Do you have copies to be distributed?

Mr. PATON: Certainly, they are ready for distribution.

The CHAIRMAN: In view of the question raised by Mr. Gilbert you are saying you have this information only for personal instalment loans but not for the other categories?

Mr. PATON: That is right, sir. We have no statistical records and I stand to be corrected, along the lines you suggest, Mr. Gilbert, on the basis solely that the rate of interest on these loans currently is 6 per cent and that is the only charge attributable to the lending area.

Mr. GILBERT: Could you give me your best educated guess, from your wide experience and that of the other gentlemen, with regard to the low range and high range on personal loans?

Mr. COLEMAN: The range is  $9\frac{1}{2}$  to 11 per cent. I think it has been that for the last five years.

Mr. GILBERT: On personal loans?

Mr. COLEMAN: Consumer loans, you asked, Mr. Gilbert for consumer loans?

Mr. GILBERT: Yes.

Mr. COLEMAN: It is approximately  $9\frac{1}{2}$  to 11 per cent.

Mr. GILBERT: What is the range on personal loans?

Mr. COLEMAN: The 6 per cent is the maximum we may charge. It is also the prime rate today. No one gets a commercial loan under 6 per cent. There are some government guaranteed loans under 6 per cent, such as student loans, farm improvement loans and perhaps a few others.

Mr. GILBERT: Thank you, Mr. Coleman. Now my next question is, under section 91 we have the word "interest" and it is not defined. Under section 93(3) we have the word "charges" on keeping an account and that is not defined. Could we direct our minds to the definition of interest. Mr. Coleman, you said during the course of the evidence that interest in your definition is the cost of the money you borrow. Is that the definition?

Mr. COLEMAN: I think I said the rate of interest that a bank charges is determined by the cost of money.

Mr. GILBERT: The cost of money?

Mr. COLEMAN: Yes.

Mr. GILBERT: Is that what interest is in Section 91? Is that what the word "interest" means in Section 91?

Mr. COLEMAN: Interest in Section 91 means the rate that a bank charges a borrower on loans.

An hon. MEMBER: The rental, to put it correctly.

Mr. COLEMAN: That is right.

Mr. GILBERT: It is the cost of the money. Does it mean anything else?

Mr. COLEMAN: No, it means nothing else.

Mr. GILBERT: What does the word "charge" or "charges" mean in Section 93(3)?

Mr. COLEMAN: Well, Mr. Gilbert, this refers to the activity charges, the operating charges of the conduct of the account.

Mr. GILBERT: Could you give me those different items that you would take into account with regard to charges?

Mr. COLEMAN: Surely. You may be running a grocery store where you have taken a lot of silver and you bring in deposits and these deposits take a lot of time to process. This takes time. Basically it is based on the time that it takes to perform the service.

Mr. GILBERT: What else does it include?

Mr. COLEMAN: It includes charging the cheques to your account, reconciling your account, preparing the cheques to return them to you, talking to you about your business. It might be an account where you come in and talk to the bank manager perhaps once a week and spend an hour or so. This all takes time.

The CHAIRMAN: You mean that when you come in and pass the time of day with your bank manager it costs you money?

Mr. COLEMAN: Almost the same as the legal profession.

The CHAIRMAN: Mr. Coleman, at least the legal profession are straightforward enough to send an itemized account.

Mr. GILBERT: Mr. Coleman, have you finished your definition of—

Mr. COLEMAN: Well, no, there might be such things as par privileges on cheques. You might be issuing cheques which are payable at par at certain other points; these have to be paid for either, as I have said before, by a service or by the maintenance of an adequate balance. I see in the report here transfer of funds or collection of funds, although usually in the collection of funds we get paid separately for that.

Mr. GILBERT: Does it include fines?

Mr. COLEMAN: Fines—F-I-N-E-S?

Mr. GILBERT: That is correct.

Mr. COLEMAN: For what?

Mr. GILBERT: Possibly for NSF cheques.

Mr. COLEMAN: No, there is a separate charge on NSF cheques.

Mr. GILBERT: Does it include recording fees?

Mr. COLEMAN: Recording fees? I am not quite clear on what you mean by that, Mr. Gilbert.

Mr. GILBERT: With regard to a chattel mortgage, suppose you took back a chattel mortgage.

Mr. COLEMAN: Possibly. If it took time to have this effected there would be a registration charge. Yes, I think it probably would include that.

Mr. GILBERT: With regard to mortgages, will they include legal fees in the future?

Mr. COLEMAN: Legal fees are set out separately, I think, and the bank would not get any benefit from the legal fees.

Mr. GILBERT: You have given us the full definition of charges as related in Section 93 (3).

Mr. COLEMAN: Well, perhaps, not a full definition but a partial one, at least, Mr. Gilbert.

Mr. GILBERT: Are you prepared to give us a full definition?

Mr. COLEMAN: Well, I do not know if I can recall to mind all the services the bank provides for a customer. I think these are pretty well known. I have attempted to mention some of them. Certification charges for cheques, that is right. Mr. Sharwood says safety deposit boxes, but you pay a rental for that.

Mr. GILBERT: Mr. Paton, would you have any objection if the word "interest" was included in the definition section and the word "charges" was included in the definition section of this act?



Mr. PATON: To define what is meant by interest?

Mr. GILBERT: Yes, and what "charges" is meant.

Mr. PATON: I think it would probably be a lot easier to include interest but it would not be very feasible to include what constitutes services because this is not a limited area. Over the next 10 years there will be additional services that we hope we can develop and devise so that it would be somewhat the same as perhaps the definition on banking. You might limit the freedom for banks to develop new services or service charges for new developments.

Mr. GILBERT: Let us get to the word keeping an account. What is meant by an account in bank terms? It says in Section 93 (3): "—charge or receive any sum for the keeping of an account—". Now, what is meant by "account"?

Mr. PATON: Keeping an account with the bank is having your name on the books of the bank. It is conceivable that it might be a loan account but it is unlikely that you would have a loan account without a deposit at all. In general the reference to an account would refer to accounts held by an individual or corporation with the bank in their name.

Mr. GILBERT: Would you have any objections to the definition of an account being set forth in the definition section?

Mr. PATON: I cannot particularly see the merit, Mr. Gilbert, but we—

Mr. GILBERT: Well, it relates to charges in section 93(3); it says, the charges in relation to keeping an account.

Mr. PATON: I think usage could very well account for—

The CHAIRMAN: Mr. Gilbert, I am prepared to let you proceed until six o'clock. Quite a large portion of your time has yet to go and I am just wondering whether you feel this was a convenient time to adjourn.

Mr. GILBERT: There is just one point to make, Mr. Chairman, and that is this: I notice in the Porter Commission they express a desire to have the total costs of the loans or the effective rate expressed in a percentage basis. What are your views with regard to that? When I talk about the total costs of loans I take into account the interest as set forth in Section 91(1) and the service charges in Section 93(3). The Porter Commission has said that the total cost of a loan should be expressed in a percentage basis. Do you have any objection to that?

Mr. PATON: I think we have already on record—referring to consumer finance loans, Mr. Gilbert, that we have no objection whatsoever to disclosing the effective cost expressed in a rate of interest basis provided that a suitable formula can be worked out and that other lenders would also be included. This provision is a natural one, in that we would expect all lenders to be in the same position. I think there is some current situation—Mr. Elderkin might be the best one to answer—in connection with the proposed amendments to that. Mr. Elderkin?

Mr. ELDERKIN: There will be a relevant amendment which is at the present time being studied.

Mr. FULTON: Related to what, Mr. Elderkin?

Mr. ELDERKIN: The total cost of the loan.

Mr. FULTON: Amendment to the Bank Act?

Mr. ELDERKIN: Yes.

The CHAIRMAN: I believe the Minister of Finance in his speech on the second reading of the bill made reference to that and I presume that details will be available to us in the course of our study as I think they should be.

Mr. FULTON: Like the deposit insurance?

The CHAIRMAN: I note that you define your consent to personal loans. Would you have any objection to commercial loans being expressed on the same basis?

Mr. PATON: I fail to see the advantage that would be gained. I doubt whether there is a general interest in having interest rates disclosed on all kinds of loans. The notes they sign are straight notes and in the majority of cases demand notes of interest are probably the most usual form of evidence of indebtedness. It shows the rate of interest effective or applicable to that particular item and that is the only charge that the individual pays on a note of that kind. When that note is repaid—the general usage is to have it on demand and at the borrower's pleasure it can be repaid—he pays interest on it to the date of the repayment. These are notes of another nature called time notes—as we refer to them in banking terms—a three month or six month note of a business corporation is not at all uncommon. But, once again the rate of interest is evidenced right on the note.

Mr. GILBERT: Just one short question: Do compensating balances take into account two factors: One, the service charges, and, two additional costs of the loans.

Mr. PATON: Service charges and the cost of operating the loan account—I want to make sure that we are not conflicting at the last minute here, with what we have said before with respect to these things. In other words, I do not want to speak too quickly.

Mr. COLEMAN: Mr. Gilbert, I have talked a lot about this but one of my colleagues reminded me that I omitted a very important point. That is, that in thousands of accounts that we have which maintain compensating balances, there are no loans. Our largest accounts probably that maintain compensating balances have no loans.

Mr. GILBERT: Well, the lead up question on that is: On the ones that you do have loans with regard to compensating balances, do they include those two factors?

Mr. COLEMAN: No. The interest rate covers the loan.

The CHAIRMAN: Do you allow interest on the deposits in the accounts in which you charge compensation balances?

Mr. COLEMAN: Which would stipulate the account?

The CHAIRMAN: Yes.

Mr. COLEMAN: As a rule, no, unless they were in a savings account; but, as a rule, I would say it would be the rare case because one would defeat the other. If you require compensating balances you could hardly pay interest because the compensating balances would take care of the activities.

The CHAIRMAN: We will continue with that, I am sure—

Mr. GRÉGOIRE: Before we adjourn may we have a copy of the statement made—

The CHAIRMAN: I should explain that through some inadvertency the bankers left the copy of this table elsewhere. They are going to provide it to the clerk first thing next week and she will distribute it.

I would like a motion, now that we have had a chance to look at the additional paper headed "Some brief comments on the profitability of the Canadian banking industry" submitted by the Bankers' Association whether we should incorporate this in our proceedings.

Mr. LAMBERT: I so move.

Mr. MORE (*Regina City*): I second the motion.

Motion agreed to.

The CHAIRMAN: It is moved by Mr. Lambert and seconded by Mr. More that we are agreed to have this form included. This is the paper submitted by the Bankers' Association having some brief comment on the profitability of the Canadian banking industry. I declare the meeting adjourned until next Thursday morning at 11 o'clock.



## APPENDIX O

## Exhibit No. 18

CLASSIFICATION OF LOANS IN CANADIAN CURRENCY  
OFTHE CHARTERED BANKS OF CANADA  
AS AT SEPTEMBER 30, 1966Compiled from returns made pursuant to section 107 of the Bank Act  
(R. B. Bryce, D/M of Finance)

	Number of Accounts	Millions of Dollars
<b>1. GOVERNMENT AND OTHER PUBLIC SERVICES</b>		
(1) Provincial governments.....	41	121.7
(2) Municipalities and school corporations.....	4,630	562.4
(3) Religious, educational, health and welfare institutions..	7,439	296.6
Total Government and Other Public Services.....	12,110	980.7
<b>2. INVESTMENT DEALERS AND BROKERS</b>		
(1) Investment dealers, day-to-day, secured.....	90	267.5
(2) Investment dealers, call and short, secured.....	333	136.9
(3) Stockbrokers, call and short, secured.....	432	90.1
Total Investment Dealers and Brokers.....	855	494.5
<b>3. PERSONAL</b>		
(1) Individuals, for other than business purposes		
(a) On the security of Canada Savings Bonds at the agreed rate for the issue.....	89,479	22.7
(b) On the security of marketable stocks and bonds...	156,580	521.0
	246,059	543.7
(2) Individuals, for other than business purposes		
(a) For Home Improvement, under the National Housing Act.....	56,149	7.53
(b) On the security of motor vehicles.....	419,923	649.6
(c) On the security of other household property.....	88,871	87.5
(d) Repayable by instalments, not elsewhere classified.	824,207	810.3
(e) Repayable otherwise, not elsewhere classified.....	516,626	822.4
Total Personal.....	2,151,835	2,988.8
<b>4. AGRICULTURAL, INDUSTRIAL AND COMMERCIAL</b>		
(1) Agriculture		
(a) Farmers, under Farm Improvement Loans Act...	164,546	403.7
(b) Farmers, not elsewhere classified.....	175,773	483.7
	340,319	887.4

## (2) Industry

(a) Chemical and rubber products.....	813	122.1
(b) Electrical apparatus and supplies.....	1,542	160.3
(c) Food, beverages and tobacco.....	6,138	359.7
(d) Forest products.....	6,253	264.6
(e) Furniture.....	1,344	48.4
(f) Iron and steel products.....	3,282	342.9
(g) Mining and mine products.....	1,453	155.0
(h) Petroleum and products.....	924	162.1
(i) Textiles, leather and clothing.....	4,052	333.2
(j) Transportation equipment.....	1,574	177.6
(k) Other products.....	5,218	194.0
	<hr/> 32,593	<hr/> 2,319.9

## (3) Public utilities, transportation and communication companies

(a) Guaranteed by a province.....	238	57.2
(b) Other.....	6,620	318.0

(4) Construction contractors.....	6,858	375.2
(5) Grain dealers and exporters.....	21,409	483.1
(6) Instalment and other finance companies.....	726	328.2
(7) Merchandisers.....	963	359.4
(8) Other business.....	73,357	1,272.6
	94,052	1,534.8

Total Agricultural, Industrial and Commercial	<hr/> 570,277	<hr/> 7,560.6
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TOTAL LOANS IN CANADIAN CURRENCY (Other than mortgages and hypothecs insured under the National Housing Act, 1954).....

2,735,077	12,024.6
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OTTAWA,

November 3, 1966.

Exhibit No. 19

CLASSIFICATION OF DEPOSIT LIABILITIES PAYABLE TO THE PUBLIC  
IN CANADA IN CANADIAN CURRENCY

OF

THE CHARTERED BANKS OF CANADA  
AS AT SEPTEMBER 30, 1966

Compiled from returns made pursuant to section 108 of the Bank Act  
(R. B. Bryce, D/M of Finance)

NUMBER OF DEPOSIT ACCOUNTS OF THE PUBLIC IN CANADA IN CANADIAN CURRENCY	Personal Savings Deposit Accounts	Other Deposit Accounts of the Public	Total Deposit Accounts of the Public
Accounts of less than \$100.....	7,158,103	1,560,210	8,718,313
Accounts of \$100 and over but less than \$1,000.....	3,993,666	1,199,303	5,192,969
Accounts of \$1,000 and over but less than \$10,000.....	2,132,781	478,727	2,611,508
Accounts of \$10,000 and over but less than \$100,000 ..	134,632	91,865	226,497
Accounts of \$100,000 and over.....	1,936	9,532	11,468
Total.....	13,421,118	3,339,637	16,760,755

DEPOSIT LIABILITIES PAYABLE TO THE PUBLIC IN CANADA IN CANADIAN CURRENCY	Amounts in Thousands of Dollars
Personal savings deposit liabilities.....	10,387,606
Other deposit liabilities payable to the public.....	7,849,860
Total.....	18,237,466

OTTAWA,

November 3, 1966.



## APPENDIX P

SOME BRIEF COMMENTS ON THE  
PROFITABILITY OF THE CANADIAN  
BANKING INDUSTRY

(By The Canadian Bankers' Association).

Evidence already placed before you by the Governor of the Bank of Canada has indicated the more rapid growth of the "near banks" during the past decade in comparison with the chartered banks. In reply to a question the Governor also remarked on the number of new "near banks" which commenced operations during the period under review. Capital is attracted where it will receive the best return and the relative profitability of other industries compared to chartered banking has obviously interested new investors.

The Royal Commission shows the following figures for net profits as a percentage of total assets and return on equity for the 1961 fiscal year:—

	Chartered Banks	Trust Cos.	Sales Finance Cos.
Net profits after taxes and all other charges expressed as a percentage of total assets	.45%	.87%	1.39%
Return on equity .....	8.8 %	10.6 %	11.0 %

(see page 368 of the Royal Commission Report)

There are 114,000 shareholders in the Canadian chartered banks and quite evidently the Government feels that it is politic that there be an even wider distribution of shares among individual Canadians (see *Hansard* May 18, 1965, page 1432).

The annual after tax return on the shareholders' equity for the Canadian chartered banks has averaged 6.79 per cent over the eleven-year period 1954/64 and 7.14 per cent over the five-year period 1960/64 (see Schedule A). When compared with seventeen other industries whose average return ranged from 3.45 per cent to 12.70 per cent (1960/64), the chartered banks (7.14 per cent) rank in the bottom 22 per cent. It is interesting to note that the return for chartered banks has been below the trust company sector, finance companies, public utilities (excluding 1958) and the composite average of all industries for each of the eleven years (1954/64). It is true that returns on shareholders' equity in different businesses are not wholly comparable, but they are indicative.

In addition to the evidence set out in the various Schedules attached, the exhibit filed with you by the Inspector General (which is not exactly comparable since it shows return on average assets whereas the attached figures are based on year-end figures) indicates an extremely slow improvement in return on shareholders' equity, mostly arising out of a declining ratio of shareholders' equity to total assets. The deteriorating overall profit margins are more clearly indicated by the ratio of net profits to average assets which has decreased from .42 in 1960 to .38 in 1965.

This low return on investment has also been reflected in the market price of the common stock. If it is assumed that 100 shares of each of any chartered bank were purchased at the average price in 1959 and sold at the average price in 1963, the time adjusted return on the original investment in 1959, including the four years of dividends, would have been approximately 6 per cent. This rate when compared to a return of 13 per cent for General Motors Corporation, 15 per cent for Du Pont of Canada and 14 per cent for Investors' Syndicate again indicates that the banks are well below other large companies.

Further investigation reveals that the bank common stock index increased at an average annual compounded rate of 2 per cent from 1959/64 (see Schedule B) which is the second lowest growth rate out of eighteen major industries. Other annual rates ranged from a high of 17.0 per cent for textile and clothing stocks to a low of 1 per cent for electric power firms. It is interesting to note that the annual share index growth rate for banks (2.0 per cent) and investment and loan companies (5.5 per cent) is below public service industries such as telephone (7.5 per cent) and all public utilities (7.0 per cent). Bank shareholders are evidently suffering in comparison with shareholders of other industries and these include many people who look upon dividends on bank stocks as a source of income in their old age.

In addition the relatively lower profit performance of the Canadian chartered banks may present problems if and when they have to raise more capital during the next decade. The more sophisticated investor of today is not so much concerned about the safety of bank stock as he once was and is more interested in an adequate return. Approximately 75 per cent of net bank earnings are now paid out in dividends so there is little room to increase dividends so as to make the shares more attractive to the investing public.

SCHEDULE A  
RETURN ON SHAREHOLDERS EQUITY—CANADIAN CORPORATIONS  
(After Tax, 1954-64)

Industry	1954	1955	1956	1957	1958	1959	1960	1961	1962	1963	1964	Average	
												11 Year	5 Year
												1954-64	1960-64
Oils and Pipelines.....	10.74	12.08	11.35	11.06	6.71	7.07	8.01	8.89	7.72	8.09	8.86	9.08	8.30
Beverages.....	11.57	10.16	8.58	9.23	8.74	8.90	8.90	8.98	8.93	8.60	8.84	9.25	8.85
Chemicals and Allied Products.....	7.68	10.40	10.55	9.25	7.55	9.24	8.82	9.15	10.90	10.85	12.41	9.70	10.43
Construction.....	13.67	13.81	12.19	10.71	10.35	8.68	6.72	6.98	8.47	7.12	9.01	9.76	7.65
Electrical Equipment.....	7.55	6.37	9.55	10.30	8.28	7.87	5.67	6.75	6.65	8.45	9.64	7.89	7.43
Food.....	7.75	8.88	8.57	8.72	8.82	9.38	8.47	8.88	8.67	9.47	10.46	8.90	9.18
Iron and Steel.....	8.68	10.05	11.15	8.84	7.97	9.38	6.26	6.28	8.44	9.43	9.79	8.78	8.05
Merchandising.....	7.24	7.15	9.23	9.69	10.07	9.40	8.50	8.59	7.91	9.11	9.78	8.80	8.75
Milling and Grain.....	6.63	5.68	5.71	5.91	6.92	9.42	9.52	6.31	5.72	5.87	8.11	6.89	7.10
Non-ferrous Metals.....	15.39	18.94	18.16	14.68	7.77	11.87	12.69	12.23	12.34	11.55	14.70	13.65	12.70
Public Utilities.....	7.49	7.58	7.67	6.90	6.31	7.29	6.66	7.21	7.29	7.41	7.73	7.25	7.25
Pulp, Paper and Lumber.....	13.40	14.70	13.90	9.35	8.15	9.45	9.55	9.65	11.06	10.90	11.87	11.05	10.60
Textiles.....	3.46	2.11	6.06	5.67	5.53	6.69	6.91	7.20	6.76	8.80	10.11	6.30	7.95
Transportation.....	9.16	4.81	5.51	4.81	3.47	3.31	2.95	3.20	3.18	3.92	4.02	4.35	3.45
Miscellaneous.....	9.47	11.76	13.69	9.91	9.37	10.05	9.80	9.68	10.01	8.55	7.70	10.00	9.15
Trust Companies.....	7.45	8.30	8.12	8.22	9.21	8.70	9.15	8.39	8.49	8.19	8.92	8.47	8.60
Finance Companies.....	15.10	14.10	13.35	12.40	12.90	12.20	12.25	11.80	10.35	9.30	10.30	12.20	10.80
Chartered Banks.....	6.46	6.67	6.47	6.39	6.59	6.44	6.86	6.88	7.22	7.23	7.49	6.79	7.14
Composite average—total companies.....	9.24	9.64	9.98	9.00	8.05	8.61	8.20	8.18	8.35	8.49	9.42	8.83	8.55
Number of companies.....	379	379	379	355	355	311	288	288	318	318	318		

Source: Annual Financial Statements—Shareholders' Report.



SCHEDULE B  
INDEX NUMBER OF COMMON STOCK PRICES  
(1959-64)

	1959	1960	1961	1962	1963	1964	Average annual growth rate (compounded) %
Investors total.....	110.4	104.5	132.7	127.9	136.7	160.3	7.5
Industrial total.....	106.8	101.7	130.0	125.5	134.4	163.6	8.5
Food.....	140.2	127.3	175.5	163.5	173.8	190.9	6.5
Beverage.....	122.6	117.5	159.5	174.4	191.2	219.6	12.0
Textile and clothing.....	130.7	114.5	134.4	153.7	212.2	291.9	17.0
Pulp and paper.....	101.5	100.2	117.0	118.6	129.9	161.8	9.5
Printing and publishing.....	220.9	253.4	326.4	300.6	312.5	326.4	8.5
Primary metal.....	95.2	87.6	98.4	86.4	96.4	118.6	4.5
Metal fabricating.....	104.6	82.6	93.8	92.3	107.6	136.5	6.0
Petroleum.....	87.1	78.2	102.6	101.7	99.2	115.0	12.0
Chemicals.....	96.9	84.2	89.1	102.3	129.6	166.8	5.5
Retail trade.....	175.9	142.5	177.3	157.3	176.0	229.0	7.0
Total utilities.....	109.7	104.7	125.8	123.1	135.9	153.7	9.0
Pipeline.....	117.2	106.2	136.4	141.1	152.7	178.6	11.0
Transport.....	88.7	76.6	83.7	83.2	101.7	149.0	7.5
Telephone.....	90.5	97.7	117.0	117.9	124.1	130.8	1.0
Electric power.....	126.0	116.3	128.6	110.6	126.0	132.3	3.5
Total finance.....	128.6	117.3	154.3	145.6	148.8	152.5	2.0
Banks.....	129.0	116.0	142.2	136.1	141.2	143.6	5.5
Investment and loan.....	127.8	119.8	177.1	163.3	163.1	169.1	

SOURCE: D. B. S. Statistics.  
Prices and Price Indexes.

## SCHEDULE C

RATE OF RETURN OF NET WORTH OF THE LEADING  
U.S. CORPORATIONS, SELECTED INDUSTRIES  
(%)

Year	Com- mercial Banks*	Public Utilities	Con- struction	Service	Manu- facturing	Moving	Trade	Sales Finance Companies	Real Estate
1952.....	7.9	9.0	13.06	11.1	12.3	10.1	10.1	15.7	12.5
1953.....	7.8	9.2	13.2	11.0	12.5	8.1	9.9	16.4	9.5
1954.....	9.3	9.3	12.2	11.4	12.4	7.9	10.0	16.4	11.3
1955.....	7.9	9.7	12.6	12.4	15.0	11.9	11.1	16.6	10.1
1956.....	7.7	9.8	14.5	13.8	13.9	13.8	11.3	16.3	8.6
1957.....	8.3	9.6	16.4	12.7	12.8	9.7	10.9	15.8	8.4
1958.....	9.7	9.7	12.6	8.4	9.8	7.0	10.2	14.6	8.3
1959.....	7.9	10.1	11.8	10.4	11.6	8.0	11.5	18.7	11.2
1960.....	10.1	9.9	1.4	9.1	10.5	7.3	10.4	13.9	9.4
1961.....	9.6	9.9	8.7	10.4	10.1	8.6	10.2	13.0	8.3
1962.....	8.9	10.0	11.4	10.8	10.9	8.8	10.1	11.9	10.4
1963.....	9.0	10.2	9.5	10.5	11.5	8.8	10.1	11.8	6.8
1964.....	8.8	10.7	9.6	12.4	12.7	10.4	12.1	12.0	7.7

\*Federated Reserve Member Bank.

SOURCES: First National City Bank of New York, Monthly Economic Letter.  
Board of Governors of the Federal Reserve System.





OFFICIAL REPORT OF MINUTES  
OF  
PROCEEDINGS AND EVIDENCE

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LÉON-J. RAYMOND,  
*The Clerk of the House.*

HOUSE OF COMMONS

First Session—Twenty-seventh Parliament

1966

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STANDING COMMITTEE

ON

FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. HERB GRAY

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MINUTES OF PROCEEDINGS AND EVIDENCE

No. 24

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THURSDAY, NOVEMBER 17, 1966

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Respecting

Bill C-190, An Act to amend the Bank of Canada Act.

Bill C-222, An Act respecting Banks and Banking.

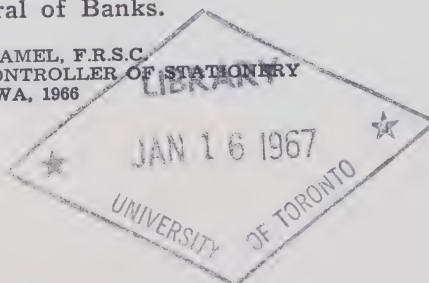
Bill C-223, An Act respecting Savings Banks in the Province of Quebec.

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WITNESSES:

*From the Canadian Bankers' Association:* Messrs. S. T. Paton, President; Leo Lavoie, Vice-President; J. H. Coleman, Vice-President; W. J. Dixon, Deputy General Manager, Bank of Nova Scotia; R. M. MacIntosh, Joint General Manager, Bank of Nova Scotia. *And also:* Mr. C. F. Elderkin, Inspector General of Banks.

ROGER DUHAMEL, F.R.S.C.  
QUEEN'S PRINTER AND CONTROLLER OF STATIONERY  
OTTAWA, 1966



STANDING COMMITTEE  
ON  
FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. Herb Gray

*Vice-Chairman:* Mr. Ovide Laflamme

and Messrs.

Addison,	Comtois,	Latulippe,
Basford,	Flemming,	Lind,
Cameron ( <i>Nanaimo-</i>	Fulton,	McLean ( <i>Charlotte</i> ),
<i>Cowichan-The Islands</i> ),	Gilbert,	Monteith,
Cashin,	Irvine,	More ( <i>Regina City</i> ),
Chrétien,	Johnston,	Munro,
Clermont,	Lambert,	Valade,
Coates,	Lamontagne,	Wahn—(25).

Dorothy F. Ballantine,  
*Clerk of the Committee.*



ORDER OF REFERENCE

TUESDAY, November 15, 1966.

*Ordered*,—That the name of Mr. Latulippe to substituted for that of Mr. Langlois (Mégantic) on the Standing Committee on Finance, Trade and Economic Affairs.

*Attest.*

LÉON-J. RAYMOND,  
*The Clerk of the House of Commons.*



## MINUTES OF PROCEEDINGS

THURSDAY, November 17, 1966.

(43)

The Standing Committee on Finance, Trade and Economic Affairs met at 11:10 a.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Cameron (*Nanaimo-Cowichan-The Islands*), Chrétiën, Clermont, Comtois, Flemming, Gilbert, Gray, Johnston, Laflamme, Lambert, Latulippe, Lind, McLean (*Charlotte*)—(13)

*Also present:* Mr. Grégoire.

*In attendance:* Messrs. S. T. Paton, President, The Canadian Bankers' Association and Vice-President and Chief General Manager, The Toronto-Dominion Bank; Leo Lavoie, Vice-President, The Canadian Bankers' Association and Vice-President and General Manager, La Banque Provinciale du Canada; J. H. Coleman, Vice-President, The Canadian Bankers' Association and Chief General Manager, The Royal Bank of Canada; W. T. G. Hackett, General Manager (Investments), Bank of Montreal and Chairman of Canadian Bankers' Association Bank Act Revision Committee; Gilles Mercure, Assistant General Manager, La Banque Provinciale du Canada; F. L. Rogers, Economic Adviser, The Bank of Nova Scotia and Chairman, Canadian Bankers' Association Economists Committee; W. J. Dixon, Deputy General Manager, Bank of Nova Scotia; R. M. MacIntosh, Joint General Manager, Bank of Nova Scotia; J. H. Perry, Executive Director, The Canadian Bankers' Association; C. F. Elderkin, Inspector General of Banks; Miss M. R. Prentis and Mr. Denis Baribeau, research assistants.

The Committee resumed consideration of the banking legislation.

On motion of Mr. Clermont, seconded by Mr. Flemming,

*Resolved*,—That the paper entitled *Table of Costs for a Personal Instalment Loan or Advance In the Principal Amount of \$1,000 Repayable in Approximately Equal Monthly Instalments as Indicated*, referred to at the last meeting and later distributed to members, be attached as an appendix to this day's Minutes of Proceedings and Evidence. (*See Appendix Q*).

Messrs. Paton, Coleman and Dixon were questioned.

In reply to a question by Mr. Gilbert, Mr. Paton referred to a paper entitled *Some notes on the more important items of sundry bank revenues (exchange, commission, service charges, etc.)*, which was read into the record. (*See Evidence*).

In reply to a question, the witnesses agreed to table forms used by the various banks involving a charge to the customer.

At 12.55 p.m. the Committee adjourned until 3:45 p.m. this day.



## AFTERNOON SITTING

(44)

The Committee resumed at 4:00 p.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Cameron (*Nanaimo-Cowichan-The Islands*), Chrétien, Clermont, Comtois, Fulton, Gilbert, Gray, Johnston, Laflamme, Lambert, Latulippe, Lind, McLean (*Charlotte*), Monteith, More (*Regina City*), Wahn—(16).

*Also present:* Mr. Grégoire.

*In attendance:* The same as at the morning sitting.

A quorum not being present, the Committee proceeded to hear evidence informally.

After some time, the Chairman noted the presence of a quorum and on motion of Mr. More (*Regina City*), seconded by Mr. Cameron (*Nanaimo-Cowichan-The Islands*),

*Resolved*,—That the evidence previously recorded at this sitting be incorporated as part of the official Proceedings.

Questioning of the witnesses was continued, and Messrs. Paton, Coleman, MacIntosh, Lavoie, Dixon and Elderkin were questioned.

In reply to a question by the Chairman as to whether the witnesses would identify the banks shown in Appendix Q simply as "Bank A", "Bank B", etc., the witnesses agreed to take this matter under advisement.

At 6:00 p.m. the Committee adjourned until 8:00 p.m. this day.

## EVENING SITTING

(45)

The Committee resumed at 8:20 p.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Cameron (*Nanaimo-Cowichan-The Islands*), Clermont, Comtois, Fulton, Gilbert, Gray, Johnston, Laflamme, Lambert, Latulippe, Lind, McLean (*Charlotte*), Monteith, Wahn,—(14).

*Also present:* Mr. Grégoire.

*In attendance:* The same as at the morning sitting with the exception of Mr. MacIntosh and Mr. Baribeau.

A quorum not being present, the Committee heard evidence informally.

Later the Chairman noted the presence of a quorum, and on motion of Mr. Clermont, seconded by Mr. Laflamme,

*Resolved*,—That evidence recorded earlier in this sitting be included as part of the official Proceedings.

Messrs. Paton, Coleman, Lavoie and Elderkin were questioned.

In reply to the question of the Chairman at the afternoon sitting, Mr. Paton named the banks who had provided the information shown in Appendix Q. (*See Evidence*).

The questioning continuing, at 10:00 p.m. the Committee adjourned until Tuesday, November 22, 1966 at 11:00 a.m.

Dorothy F. Ballantine,  
*Clerk of the Committee.*





## EVIDENCE

(Recorded by Electronic Apparatus)

THURSDAY, November 17, 1966.

The CHAIRMAN: Gentlemen, the meeting will come to order. When we adjourned Mr. Gilbert had the floor. However, before inviting him to continue I will invite a member of the committee to make a formal motion to include in our proceedings the various tables. The table of costs for personal instalment loan or advance and so on which was presented by the bankers' association. These were distributed to the members a few days ago but there were not sufficient copies on hand when they were first alluded to.

Mr. CLERMONT: I so move.

Mr. FLEMMING: I second the motion.

Motion agreed to.

The CHAIRMAN: Mr. Gilbert, I believe you had some time left for your questioning.

Mr. GILBERT: Mr. Chairman, last week I was directing my questions to clauses 91 and 93(3) concerning interest and bank charges and keeping an account. I would like to refer back to Section 91.

The CHAIRMAN: Could I make a suggestion? Unfortunately because of the nature of the transcription service we are using the proceedings do not come out as quickly as we all would like. If you have notes as to what was being said when we last adjourned, it may be helpful. If I recall, you asked for certain definitions.

Mr. GILBERT: Yes, definitions of interest and bank charges, and keeping an account.

The CHAIRMAN: Perhaps the witness who was replying might assist us in our deliberations today by recalling some of the answers. You do not mind me making the suggestion?

Mr. GILBERT: Not at all, Mr. Chairman. I think it was Mr. Coleman who was answering the question.

Would you give us a definition of interest, Mr. Coleman?

Mr. J. H. COLEMAN (*Vice President, the Canadian Bankers' Association*): Mr. Gilbert, I do not know if this is a very sophisticated definition but I think interest is the rental cost of money loaned. It is the rent you charge to the person borrowing the money.

Mr. GILBERT: Would "interest" and "discount", as referred to in clause 91, be one and the same thing?

Mr. COLEMAN: Substantially, but I think the term "discount" sometimes, means this: if you borrow money and the note is discounted then the borrower just gets the principal amount less the amount of the interest; that is commonly known as discounting a note. On the other hand, if you borrowed money and paid interest you might pay the interest when the note matures or you might pay it on a monthly basis.

Mr. GILBERT: Would you give me your definition of bank charges referred to in clause 93(3). What constitutes bank charges for bank services?

Mr. COLEMAN: Bank charges could cover a variety of services: operating charges for the conduct of an account, collection charges, charges for par privileges, etc. I do not know whether you would put in this category the rental for a safety deposit box. There are safekeeping charges if you just leave securities with the bank and do not put them in a box. Bank charges would cover things such as that.

Mr. S. T. PATON (*President, The Canadian Bankers' Association*): Mr. Gilbert, if I might interject, we have a statement here covering the variety of items coming under "service charges" which we would be in a position to distribute now to members of the committee.

Mr. GILBERT: I think this would be very useful.

The CHAIRMAN: Might I just ask you to wait a moment while this statement is distributed? Because it is very brief,—perhaps while it is being distributed—although we do not usually do this—it might be helpful if I asked one of our witnesses who is in good voice this morning to read this.

Mr. COLEMAN: Mr. Chairman, I did not attend the convention so I am reasonably healthy. Would you like me to read the whole thing?

The CHAIRMAN: It seems to be rather brief. Perhaps at the same time you could complete the answer you had begun while the copies are being distributed.

Mr. COLEMAN: This is headed: "Some notes on the more important items of sundry bank revenues—exchange commission service charges etc. Under the heading of "Service charges" it reads:

These are charges made to cover the cost of operating deposit accounts on behalf of customers. The charges are applied to three types of accounts as follows:

(a) Savings Accounts,

on which the customer pays 15 cents a cheque.

(b) Personal Chequing Accounts—10 cents per cheque

(c) Current Accounts—10 cents per debit and credit entry with a minimum charge of \$1 per month; or on an account analysis basis.

NOTE: In the case of savings accounts and current accounts an allowance in the form of a number of free entries is made in respect of the value of the balances maintained.

Then there is a heading "Exchange on Out-of-Town Cheques" which reads:

Cheques negotiated drawn on points outside the clearing house area are generally subject to exchange charges—

But as you know some companies pay this themselves by having what is called "negotiable without charge" privileges so the payees are not assessed this amount. Then there are domestic exchange transactions.

Instruments for the transfer of funds in Canadian currency such as Bank Money Orders, Bank Drafts, Mail Transfers, Telegraphic Transfers. . .

Then there are domestic collections. These are bills of exchange and similar items, drawn and payable in Canada, lodged for collection. There are foreign exchange transactions, these are instruments for the transfer of funds in other than Canadian currency such as bank money orders, bank drafts and so on. Then there are securities transactions, which are purchases, sales and other transactions on behalf of customers in stocks, bonds, and so on. The safekeeping of securities and the collection of income thereon—that is cutting coupons and crediting the proceeds to clients' accounts; rentals of safe deposit boxes, and there are miscellaneous services such as acceptance of payment of accounts the handling of grain drafts and documents, and a whole number of things, the handling of livestock, produce and dairy tickets, making up of payrolls and so on.

The CHAIRMAN: Thank you. I think since this has been read we will not have it incorporated as we do when documents are circulated. Perhaps, Mr. Gilbert, you could continue.

Mr. GILBERT: Thank you, Mr. Chairman. I wonder if I may direct your attention to the phrase "keeping an account" referred to in clause 93(3). Would you tell us what is meant by "keeping an account". What type of accounts are you referring to?

Mr. COLEMAN: I would say, apart from the deposit accounts a client could have with a bank, this could include a safekeeping account. It could include a loaning account—here I am thinking specifically of the consumer type loan where the customer agrees to pay a service charge over and above the 6 per cent rate of interest; any of these services, I suppose. You could, I suppose, refer to any of these services and many of them would be an account with the bank.

Mr. GILBERT: Probably I could direct my next question to Mr. Paton. Suppose I went into a bank for a consumer loan of \$100 and the bank service charges and the rate of interest amounted to \$20, so that the total loan would be \$120. Suppose I had agreed to make 12 payments of \$10 each. Would that be set forth in any clear way in any papers I would sign with regard to that loan?

Mr. PATON: Yes, Mr. Gilbert; incorporated in the note you signed would be the monthly repayment you would make.

Mr. GILBERT: Would there be shown, incorporated in that note, \$100 for the loan and the \$20 embracing the interest and the bank service charges; in other words, would I definitely know that I was paying \$120 for the \$100 I borrowed.

Mr. PATON: In every case, you would. The manner in which it is shown might vary from bank to bank but in every case you would know that you were paying \$120, that you were getting \$100, and the amount of the principal repayment monthly would also be available to you.

Mr. GILBERT: Is it right that they passed an act in Ontario with regard to showing the interest rate on consumer loans on a percentage basis?



Mr. PATON: I do not think that act has been passed. I know it is under consideration in other provinces as well as Ontario. I doubt very much if there has been any official legislation on it. I mentioned that Mr. Dixon was technically expert in this field and perhaps he might be able to give us more comprehensive answers to those particular questions. With the Chairman's permission, I will call on him.

The CHAIRMAN: Would Mr. Dixon like to advance and be seated next to his colleagues. We will give him the opportunity of being recorded for posterity.

Mr. GILBERT: Probably Mr. Dixon can bring us up to date on whether that act has been passed.

Mr. W. J. DIXON (*Deputy General Manager, Bank of Nova Scotia*): My understanding, Mr. Gilbert, is that it has not been passed in the Province of Ontario at this point.

Mr. GILBERT: What are the main terms of that proposed act, Mr. Dixon?

Mr. DIXON: I think it is to achieve the disclosure of these charges on consumer instalment loans as an effective percentage rate per annum.

Mr. GILBERT: Would this in any way affect any document that you have customers sign regarding loans that are made with the bank?

Mr. DIXON: I am sorry; I do not understand?

Mr. GILBERT: In other words, would you have to change your forms?

Mr. DIXON: No, I think there probably would be an addition to the forms to comply with the proposed manner of disclosure. There would be an addition to the forms.

Mr. GILBERT: You say there would be?

Mr. DIXON: Yes.

Mr. GILBERT: What would the addition be?

Mr. DIXON: The addition would be the manner in which it will be prescribed that we are required to disclose the effective rate per annum. I think it will be a simple phrase.

Mr. GILBERT: We are directing our minds to consumer loans; is it feasible to do the same with regard to commercial loans?

Mr. DIXON: In commercial loans I think it is fair to say that the effective rate of interest is usually stated quite clearly.

Mr. GILBERT: Are the bank charges incorporated?

Mr. DIXON: I do not think they are in the loan agreement.

Mr. GILBERT: No?

Mr. DIXON: No.

Mr. PATON: If I may intervene, the interest on a commercial loan is stated clearly in the note and there are no other charges on that amount of money borrowed from a bank other than the interest rate that is clearly indicated on the note form.

Mr. GILBERT: On any commercial loan?

Mr. PATON: Yes.

The CHAIRMAN: Mr. Gilbert, there may be a bit of confusion here. Perhaps you were going to ask this question next but, if I may interject, it was my understanding from previous discussion that commercial customers who had

loans on which interest was charged would be such that they would in some cases, if not all cases, find themselves in positions where you would ask them also to pay service charges. Did I misunderstand that aspect of our discussion?

Mr. PATON: No. I would put it this way, I think, Mr. Chairman. Where a line of credit is granted to a commercial customer a commitment fee could be charged for the availability of these funds, so that at any time he wished to avail himself of these funds they would be there for him. But it would not apply against the actual borrowings, the actual borrowings would be borrowed at the rate of interest which had been agreed to by both the customer and the bank. I am assuming normal times, when we have not just one flat rate of 6 per cent as we have currently.

The CHAIRMAN: What about these charges which were just referred to in the paper Mr. Coleman read? Would the fellow who signs the note on which an interest rate is stipulated in some cases, if not all, be asked to pay these charges as well?

Mr. PATON: On his other accounts that he is operating, his safekeeping account, his current account, his deposit account? These are the ones outlined in Mr. Coleman's paper.

Mr. COLEMAN: Mr. Chairman, these charges would not relate to the loan account; these would relate to the other features mentioned in the memorandum.

The CHAIRMAN: In what account would you possibly ask for a compensating balance?

Mr. COLEMAN: You could either pay a service charge or maintain balances which would compensate the bank. There are two ways of compensating the bank.

The CHAIRMAN: On what account?

Mr. COLEMAN: Deposit accounts.

The CHAIRMAN: Would you try and distinguish for us between a deposit account and a loan account?

Mr. COLEMAN: A deposit account is one on which a customer issues cheques and makes deposits; he gets a statement back and so on. A loan account is an account where a customer comes in and signs a note form—you are speaking of a commercial loan account now, presumably—and agrees to a certain rate of interest; the interest is charged usually, if it is a demand note—I think it is the common practice in Canada on large accounts to take demand notes on commercial accounts—monthly to the borrower's account.

The CHAIRMAN: Are loan accounts and deposit accounts never one and the same thing?

Mr. COLEMAN: No, they are not.

The CHAIRMAN: Is a loan account actually your account in a sense?

Mr. COLEMAN: The bank's account?

The CHAIRMAN: Yes, recording your credit?

Mr. COLEMAN: You could have a loan account and not have a deposit account. Of course, you know you could have a deposit account and not have a loan account. They are two completely different things.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You could have both accounts?

Mr. COLEMAN: That is right, but they would be separate accounts. One would be a loan account and one would be a deposit account. If you were borrowing by way of overdraft then your deposit account becomes a loan account.

The CHAIRMAN: I see.

Mr. COLEMAN: But this practice is not as prevalent as it was.

Mr. LIND: Do overdraft privileges still exist in some areas?

Mr. COLEMAN: They do, unfortunately, but our bank is doing our best to restrict them because we think it is a very unsatisfactory way of borrowing, both from the customer's standpoint and that of the bank.

Mr. LIND: Would you explain why?

Mr. COLEMAN: Yes. It is unsatisfactory because usually a loan by way of overdraft is not a pre-arranged loan, and the bank is faced with a request to pay a cheque which would constitute a loan frequently not knowing what the loan was for. I think any lender is entitled to discuss with a borrower why the borrower needs the money, what it is for and when it is going to be repaid. I think many of us find a lot of our bad debts originated as overdrafts.

The CHAIRMAN: I thought, Mr. Gilbert, it would be useful to clarify this. If I may ask a question for further clarification. When a customer has a loan account and a deposit account, is it right the loan account is the account in which you deposit the proceeds of the loan when it is made?

Mr. COLEMAN: No, Mr. Chairman. When the loan is made we open what I think most banks refer to as a liability account and that is a loan account. The proceeds are deposited to the deposit account so the customer can issue cheques and distribute or disburse the proceeds.

The CHAIRMAN: And what happens when payments are made on the loan?

Mr. COLEMAN: It goes on the liability account, it has nothing to do with the deposit account. Sometimes the customer will say, take \$100 a month or \$1,000 a month out of my deposit account and apply it on loans. That would be the only time there would be a direct relation. It would be a debit to the deposit account and a credit to the loan account.

The CHAIRMAN: So in a sense the loan account is an asset item on your books for you?

Mr. COLEMAN: Absolutely; it is one of our assets.

The CHAIRMAN: And the deposit account is a liability.

Mr. COLEMAN: I think it is well that that was brought out because I think there is considerable confusion in the minds of a lot of people. I know—I was with the bank a long while before I realized a deposit account was a liability; I thought it was an asset.

The CHAIRMAN: If I grasp that point I will thank my lecturers in economy at McGill School of Commerce.

Mr. COLEMAN: As you know, if you deposit money with us we have a liability to you to pay it back, and that is what it amounts to. On the other side of the balance sheet we have cash, investments and loans, and these are like accounts receivable on a company's balance sheet.



The CHAIRMAN: Would you trace the transaction involving the charging of interest on a loan.

Mr. COLEMAN: Yes. As I said before, Mr. Chairman, in large commercial accounts and in small commercial accounts as well, I think the common practice, certainly in our bank, is to put these notes on a demand basis and to debit the interest monthly to the customer's account. Sometimes a customer prefers to make a note out for three months or six months, at which time the interest is added, and he knows when he signs the note the total amount he eventually has to pay back. That is, the principal plus the interest.

The CHAIRMAN: In fact, you take the money out of his deposit account for the interest and apply it against his loan account.

Mr. COLEMAN: That is correct, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): May I ask you a supplementary question, Mr. Coleman? Would a customer with a deposit account be required to keep a compensating balance before he would be allowed to open a loan account.

Mr. COLEMAN: Mr. Cameron, I would say that we have thousands of accounts on our books where compensating balances are maintained and there are no loan accounts.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would you repeat that, please.

Mr. COLEMAN: I would say that we, and probably all the banks, have thousands and thousands of accounts on our books where compensating balances are maintained to take care of the activity of the account and where there are no loan accounts. As an example, take a large paper company that issues thousands of cheques a year but has a heavy cash flow and does not need to borrow; we insist that we have to be compensated one way or another. They must maintain compensating balances or pay us an agreed amount as a service charge, which is determined by an analysis of the account.

The CHAIRMAN: I also assume that there are situations where you have loan accounts and deposit accounts for which you require compensating balances.

Mr. COLEMAN: Oh, there are many, yes, but the compensating balances relate to the work involved on the bank's part in carrying the account.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): How do you estimate the compensating balances issued.

Mr. COLEMAN: The cost of money.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): That is rather vague, Mr. Coleman.

Mr. COLEMAN: Well, I mean if money is worth, let us say, 5 per cent, and we have a compensating balance of \$100,000; that money is worth \$5,000 a year to the bank.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Coleman, the cost of money does not at all enter into the picture which you mentioned just now of the large company that maintains a balance and is issuing a large number of cheques. You must have some other yardstick for deciding what compensating balance they have there.

Mr. COLEMAN: Mr. Cameron, I would say with respect that the cost of money does enter into it there because the way we determine the balance that needs to be kept is to count the number of cheques, the number of payrolls, all the services that we provide for that account. Let us assume that the cost for operating the large hypothetical account that has been referred to is \$30,000 a year, then we would have to ask that company to maintain balances sufficient to return to us at a rate we consider reasonable to compensate us to the extent of \$30,000 a year plus a built in profit.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well, is that not the cost of labour you are talking about. Mr. Coleman, I must say I find it very difficult to understand your use of the term "cost of money."

Mr. COLEMAN: Mr. Cameron, perhaps you would suggest that I should say "the worth of money"—what money is worth today.

The CHAIRMAN: You are therefore exacting an interest rate in that account if you say cost or worth of money. You just defined earlier to Mr. Gilbert that interest is the cost of money.

Mr. COLEMAN: Well, Mr. Chairman, I do not think there is a direct relation.

The CHAIRMAN: Well, perhaps we should let Mr. Gilbert continue.

Mr. LAMBERT: Mr. Chairman, I hope I can express my view on this. In the handling of a large turnover account, the bank is, because of the time lag, charging up the cheque against the account and is somewhere else advancing the money by paying that cheque. The bank itself is involved to the extent of, say, maybe having a \$100 out with pieces of paper in transit and the bank, in actual practice—that is the reason why there are clearing charges—itself has advanced the money out on behalf of the customer and then is compensated when it charges the cheque to the account. There are anywhere up to two days to seven days in which the bank can advance money to the public at large with regard to this customer. Therefore, it must reckon what is the cost of that money to it.

Mr. COLEMAN: Mr. Lambert, this is the float that we talked about the other day. I think that it is estimated that the total float of all the banks is currently about one billion dollars a year—that is money that has been turned over to customers and other banks—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Does that constitute the sole yardstick you use for compensating balances—the sole yardstick you use?

Mr. COLEMAN: Oh, no. There are various ingredients making up the final cost.

The CHAIRMAN: Mr. Paton, I think, wants to offer some information that he feels may be helpful.

Mr. PATON: On our lending functions our association has produced total costs. These clerical and administrative costs are typical of the operations involved in the lending function of the banks. It was \$119,000,000 in 1965, 22 per cent of the total clerical and administrative costs of the banks. In other words, 22 per cent of our complete overhead was attributable to our lending operations.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): How do you classify the interest that I pay a bank when I make a loan? Is this again the cost of money? In other words, what I want to get clear is this: What difference is there in essence between these charges to which you give a variety of names, and an

interest charge? Now, to me, interest indicates the cost of money and I cannot see that there can be any other definition, or that there can be any cost of money that cannot be covered in an interest rate. This is the point I want to get clear.

Mr. LAMBERT: To the bank or to the customer?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): To the bank, of course.

The CHAIRMAN: I think this is our problem, if I may say so. I think both Mr. Cameron and Mr. Lambert have made useful contributions here. I think our problem may be that the bankers at various points in our discussions have attempted to limit the cost of money to the concept of getting it from the public in one way or another and, at other times, they have perhaps unwittingly attempted to relate it to the administrative or overhead costs in handling that money within their banking set-up. Now, I am not suggesting any judgment at this point whether one definition or the other is more appropriate but I think this has caused some of our problems in our discussion here.

Mr. GILBERT: Mr. Chairman, I would like to ask Mr. Paton this question. Mr. Coleman suggested that the interest rate is charged monthly to the account. Now, is the interest charged on the total amount of money borrowed or is it charged on the reduced balance every month?

Mr. PATON: On ordinary business loans—commercial loans, Mr. Gilbert, the charge is a single charge per month on the amount of money actually borrowed calculated on a daily balance. Let us assume that the customer has a loan at the beginning of the month for \$100,000; a week later it is down to \$50,000; a week later it is up to \$60,000—and it probably has 10 or 20 different balances during the month. He would pay interest at the prescribed rate on the actual amount outstanding each day. That is one form of lending and I think perhaps you are alluding to the consumer finance lending?

Mr. GILBERT: Yes. Take that example of \$100 that I borrowed at the first of January. At the first of February what am I paying interest on? Suppose I have agreed to pay \$10 per month for 12 months. What am I paying interest on on February 1? Am I still paying it on the \$100, or am I paying it on the \$100 less the amount of principal that I have paid?

Mr. PATON: Once again, we are getting into the variety of operations of one bank versus another. I think possibly Mr. Dixon could give you a concise answer to that.

Mr. DIXON: I think it is fair to say that in the case of the \$100 personal loan you are speaking of, that within the first month you will pay interest on \$100 for one month. That has been pre-calculated.

Mr. GILBERT: What do I pay on the next month?

Mr. DIXON: You pay on \$90.

Mr. GILBERT: On the \$90.

Mr. DIXON: That is right. And \$80 the next and \$70 and so on down. If you would refer to the tables which were submitted, in the case there we were using \$1,000 and you will see that the interest amount varies between \$33.13 and \$32.50, but that is 6 per cent simple interest on the reducing principal balance.



Mr. GILBERT: Would you call that simple interest?

Mr. DIXON: Yes sir.

Mr. GILBERT: On a monthly basis?

Mr. DIXON: Yes, on a monthly basis.

● (11.42 a.m.)

(Translation)

Mr. CLERMONT: Mr. Chairman, I have a supplementary question. Mr. Dixon mentioned a document that was tabled before this Committee last week in regard to consumer loans. I think that section 91 as it stands now speak of a 6 per cent maximum rate, is that right? I wonder if the banks on consumer loans charge 6 per cent, not  $5\frac{1}{2}$ , but 6 per cent. Is that right?

How is it then that in the table that you have tabled for us in regard to interest or discount rates, that no banks show the same amount for the sum of \$1,000 either for 12 months, 24 months or 36 months, if the law only allows 6 per cent and if, as I imagine, the banks charge 6 per cent for those loans, not  $5\frac{1}{2}$  but 6 per cent.

The CHAIRMAN: Mr. Dixon will give a short reply, but may I suggest to you that your question is a bit too long for a supplementary question. Perhaps we are going to have an exchange of questions, which is not proper at this stage.

Mr. CLERMONT: Mr. Chairman, if you will allow me, you have allowed supplementary questions—

The CHAIRMAN: No, no, I allow your questions, I only made a suggestion, perhaps I can't say your questions are out of order, perhaps Mr. Dixon can give an answer.

(English)

Mr. DIXON: From my understanding and my knowledge here of the interest factor shown in each one of these 8 tables, you will see they vary from \$33.13 to \$32.50 to \$31.96, and my understanding of the difference between each one is due to rounding; that is, they have actually taken either 31 days or 30 days as a month. In the first case we had of \$100, there happened to be 31 days in January, 28 days in February. There is another rule and that is taking a 360 day year. It is the few cents difference here between these sums of interest that accounts for the difference.

(Translation)

Mr. CLERMONT: Mr. Dixon, in Bank "A" for 36 months you have \$99.40, for Bank "B", you have \$92.50 for 36 months, which makes a difference of \$7.00. Can you explain this?

(English)

Mr. DIXON: Only in the same manner that I did before, sir. It is due to rounding, taking a 360 day year or a  $365\frac{1}{4}$  day year. I think we could all sit down with tables and probably come out with the same amount of difference.

The CHAIRMAN: Perhaps we should let Mr. Gilbert complete his questions.

Mr. GILBERT: I have a few short questions and then I will be finished, Mr. Chairman.

Is it true that if I were to borrow \$100 from the bank that sometimes they discount it and they would give me only \$94?

Mr. DIXON: Yes sir.

Mr. GILBERT: And then I would still pay on the \$100 loan? In other words, my interest is calculated on the \$100?

Mr. DIXON: Well, the discount was calculated on \$100; that is, discounting \$100 at 6 per cent for one year would produce \$6 and therefore it would be deducted from the \$100 note and you would receive \$94 in proceeds.

Mr. GILBERT: On January 31 of that first month, on what amount would I pay monthly interest?

Mr. PATON: Mr. Gilbert, when you received the discounted note, you are paying your total charge at the outset.

Mr. GILBERT: In advance?

Mr. PATON: Yes, and you pay no further amounts other than repaying the principal at the end of each period.

Mr. GILBERT: Have you any objection to expressing the total cost of the loan in an effective interest rate?

Mr. PATON: We are on record as saying we have no objection to expressing matters of interest cost, on the assumption that this would be the general requirement for all lenders.

The CHAIRMAN: I will now recognize Mr. Johnston, followed by Mr. Clermont, Mr. Lambert, Mr. Lind and Mr. Cameron.

Mr. JOHNSTON: Following along on the question of bank interest rates and the argument to increase the amount allowable to banks, last week as I recall we had a rather interesting exchange between Mr. Lind and Mr. Coleman on the process that would ensue if Mr. Lind applied for a loan, and we had reference to several checks that would be made before such a loan would be granted. Should the banks be permitted to increase their interest rates, would we assume that that process would change at all?

Mr. PATON: No, there would be no change in that process. The routine would be the same.

Mr. JOHNSTON: The checks would still be made?

Mr. PATON: Yes.

Mr. JOHNSTON: Could we assume then that there would be any difference in the percentage of applications rejected. Would that change?

Mr. PATON: Mr. Johnston, complete removal of the interest rate ceiling would enable the banks to take on loans with a higher risk factor, and therefore the answer to your question would be that rejections probably would be less.

Mr. JOHNSTON: You say probably; you really could not give us any assurance that they would be less.

Mr. PATON: I would: yes, we could. We have lived so long under these restrictions that we hesitate to make predictions, but the trend definitely would be, yes.

Mr. JOHNSTON: Do you think this would be any appreciable percentage of the number?

Mr. PATON: Once again, it depends entirely upon monetary conditions as to whether there is an available additional supply of funds. But I think that if the ceiling were removed, there would be an appreciable addition to the banks' participation in loans that are currently going to much higher cost lenders.

Mr. JOHNSTON: In other words, you would anticipate an increased supply of funds. Is there any relationship between these.

Mr. PATON: Yes, we would be more competitive in our ability to gather these funds.

Mr. JOHNSTON: You are not assuming though any total increase. You mean funds to the bank; you do not mean increase in the money supply?

Mr. PATON: No sir. The banks would be able to attract additional deposits with which they could make loans and participate in this area to a greater extent.

Mr. JOHNSTON: In other words, someone else would be lending less and you would be using the same pool of money?

Mr. PATON: Assuming a constant supply of funds in total then naturally if we acquired an additional share, other lenders would have less.

Mr. JOHNSTON: Considering the process which you outlined the other day—and there would be no change in that—I would assume then that a great majority of the loans that would be made, even with an increased rate, would be regarded as sound loans and would be the sort of loan that is presently used, I believe, for financing production?

Mr. PATON: Yes. Our credit judgment would not be affected.

The CHAIRMAN: Would Mr. Johnston yield to a supplementary?

Mr. JOHNSTON: Yes.

Mr. FLEMMING: Mr. Paton, would it allow you the removal of the interest ceiling rate and allow you to make what is generally known in terms of banking parlance as "term loans" to a greater extent than you do now.

Mr. PATON: Yes. The removal of the ceiling in itself would not be particularly directed towards that source, Mr. Flemming. The additional areas in which we can lend, mortgage lending and mortgage security, as the new act envisages will permit us to get into that. But the removal of the ceiling most definitely would be of assistance to us in making loans of a term nature. Normally, in banking parlance we look at two years and up as "term".

Mr. McLEAN (*Charlotte*): I would like to ask a supplementary question.

The CHAIRMAN: Again, if Mr. Johnston will yield. He signifies, yes.

Mr. McLEAN (*Charlotte*): If the interest ceiling was removed on these loans would this increase the interest rates on your other loans; that is, would you be inclined to average your interest on all loans?

Mr. PATON: If the interest rate ceiling were removed, Dr. McLean, under current monetary conditions there would be a change in the average of interest



rates; there would be a fanning out of interest rates. Under normal conditions,—and we like to think back to normal conditions when money costs were less than they are today—you would find that the average loaning rates of interest in banks would be probably less than it would be under any type of ceiling prohibition. Freedom of interest and freedom to compete, meaning an additional pool of funds into any lending area, will, have the result of reducing the average cost. This was exemplified when we went into N.H.A. lending and it also has been exemplified in consumer finance lending.

Mr. McLEAN (*Charlotte*): Would the commercial loans bear a certain amount of the increase in interest on your risk loans?

Mr. PATON: There would be no connection. I think your question is, would we charge a higher rate of interest on commercial loans to offset riskier loans that we are willing to take on perhaps at an even higher rate than the commercial loan but still not as high as we would apply to that particular loan. Any type of loan that we make would bear the interest, in our judgment, that it should carry rather than have it subsidized by any other form of lending. As to what is the rate of interest it should carry, would be a matter of individual judgment for the banks too.

Mr. JOHNSTON: In other words, would this mean then that large amounts of the money would still be loaned out at 6 per cent even though the rate had gone up to 8 per cent?

Mr. PATON: I cannot say yes to that. I think the simple fact of the matter is that the present 6 per cent rate is not a natural prime rate of lending under the current cost of funds.

Mr. JOHNSTON: It is something like a speed limit on a highway then. If you say that the maximum rate of speed is 60 miles per hour, everybody drives at 60 and very few people elect to drive at 40 or 50. If you raise your rate your loans will rise concurrently. We may be a progressive movement, in other words.

There is a strong suspicion in my mind that the increase in the lending rate, if it is allowed, is going to increase the cost of money.

Mr. PATON: To the customers?

Mr. JOHNSTON: Yes. And because so many of the customers are those who are financing production we know that people who are in the producing business can regain their costs by raising their price. Would you anticipate then, an increase in the cost of goods and the cost of living once the bank increase is permitted, if it should be permitted?

Mr. PATON: That is a difficult question to answer by yes or no.

Mr. JOHNSTON: I was not asking for a yes or no answer.

Mr. PATON: If indeed we can bring under the umbrella of bank lending, borrowers who are currently borrowing elsewhere at a higher rate of interest then automatically their charges would be reduced; therefore, the cost of their goods certainly would not be increased as the result of the participation of the banks in lending them money. In the area of other loans where perhaps the interest rate would go up, we are to a certain extent dealing in a hypothetical situation because we just do not know under what conditions we will be lending money when this interest rate ceiling removal becomes effective—although,

looking to the reasonably near future, we do not see that conditions will be too much different from what they are currently. It is also true that where borrowers have to pay more interest, and this will happen in some instances, then the cost of their goods, be they a manufacturer and so on, may be affected. In contrast to that, there will be others who will be paying less if they come under bank lending. Within a reasonably short time we would anticipate that the average cost to borrow money from the banks on behalf of all the people who borrow from them would not necessarily increase. We cannot say it would stay as it is or decrease, but it would not necessarily increase. And I do not think that the effect of it would be material in the ultimate problem that you have posed in your question, Mr. Johnston.

Mr. JOHNSTON: It remains, though, a possibility—

Mr. PATON: A possibility. We have to accept that this is so under present conditions.

Mr. JOHNSTON: —that this will add to the cost spiral and the inflationary pressures.

Mr. PATON: I would say that the possibility that it would result in heavier costs to certain classes of borrowers would have to be considered. Perhaps, Mr. Coleman might supplement that, Mr. Chairman.

Mr. COLEMAN: I might just say, Mr. Johnston, that money is similar to any commodity, sugar, for example. If the demand for sugar is great and the supply is scarce, the cost inevitably goes up. Rates find their own level. It is the law of supply and demand. And if any one of the banks charged what was an abnormally high rate an intelligent customer would not pay it; he would go to some other lender. This is what will affect the cost of money in a free system when rates are allowed to find their own level—and then it is the law of supply and demand that takes over. This applies to the interest on money just the same as it does to the cost of any commodity.

Mr. JOHNSTON: I would be very skeptical about this definition of money being simply another commodity. Automatically, it seems to me, it assumes a whole set of assumptions—the cost of money and the producer element. I think this is what Mr. Cameron was getting at earlier in our session, and I would not want to get back into that extremely complex argument. I think that you have to realize that you are swinging a pendulum here and it depends on which swing you look at because the picture changes. I do not accept the suggestion you made earlier that interest was rent on money. Again, you run into a problem. If you pay a higher rent you assume a higher standard of living, but if you pay a higher interest rate you borrow the same kind of money. In a way these comparisons are invidious to the aims of the Committee.

Mr. COLEMAN: Well, the cost of money should be different to different borrowers. If you came in with a \$100 Government of Canada bond, as security for a loan, I would say that you should get a better rate than a person who comes in with no security. But today that does not apply; the secured borrower pays the same as the unsecured borrower because there is a maximum that a bank can charge. Money really has no loyalty. We find that if we want to go out and pay high interest rates for money—and this applies to all countries—the money will come into Canada; if we do not it will go to some other country. People will put their money to work where it is to their best advantage.

Mr. JOHNSTON: Of course this might be true, but you know very well that the secured loan and the unsecured do not pay the same, especially when money becomes tight. If I do not have the security, I do not get the loan from the bank.

Mr. COLEMAN: No, that is not strictly correct, Mr. Johnston. All the banks have many, many unsecured loans on their books. It depends on the borrower's credit worthiness.

Mr. JOHNSTON: I will pop around for the address of some of those banks afterwards. I have found that it does not always work that way.

If I may change the line of questioning somewhat, do you feel that the revenues of the banks are unsatisfactory in some way at the present time? Is this part of the concern in increasing the interest rate?

Mr. PATON: Mr. Johnston, last week we circulated to the members of the Committee a statement showing the relative profitability of the banks related to other industries. It was a four or five page document which I think very clearly elucidates the comparative profitability of the banks vis-à-vis the other concerns. Our concern in getting the 6 per cent ceiling off is not tied directly into the hope that we will automatically and by virtue of this unilateral action suddenly show a substantial increase in earnings. We realize that we have operated under a serious disability in the last number of years which has precluded us from being wholly equitable to our customers on both sides of the fence, namely, the depositors and borrowers. Therefore, we would assume that with the complete removal of the interest rate ceiling we would have to re-assess our position with respect to those leaving money with us as well as those borrowing money from us.

The answer to your question is that our concern about the removal of the ceiling is not primarily related to suddenly showing a sharp upturn in earnings. We would hope that this would come from doing a larger volume of business more efficiently under a similar type of margin under which we have been operating prior to the present emergent situation.

Mr. JOHNSTON: I appreciated the sheet you have referred to and I have given it some study. Again, you have complicated the picture immensely by adding all sorts of commodity producers in your comparisons when the disability that you have just mentioned would apply really to only two of these, the trust companies and the finance companies, the only ones that you find yourselves in a disadvantageous position to and not to any of the rest in the group.

Mr. PATON: I think we are trying to relate here the attraction of bank shares to an investor, to the attraction that he could obtain investing elsewhere.

Mr. JOHNSTON: You do not have some of the other problems. For example, you have not had difficulty meeting your payroll. You have not had a strike lately in banking.

Mr. PATON: But we have had other problems that perhaps the people who have had strikes have not had. I do not think I would be unduly concerned about running into additional problems in these other industries, vis-à-vis what I run into and what the industry that we are all employed in runs into.

The CHAIRMAN: Have you had any difficulty recently in selling any of your shares, or with respect to any offerings that you have made?



Mr. PATON: No, there has been no rights offering in recent years, Mr. Gray, but I think that from this return you can see the performance of banks has not been as good as the various other classifications.

The CHAIRMAN: So far as the market is concerned, is there ever any difficulty in willing sellers finding willing buyers on the market at the price of things offered by you directly to the public?

Mr. PATON: Banks shares always have been readily marketable. At the price they are listed perhaps they might not attract very many sellers whereas if their performance had been somewhat closer to some of the others we compare them with, there could have been a greater activity in their shares.

The CHAIRMAN: Mr. Lind has a supplementary question.

Mr. LIND: When you issue shares to your present shareholders, what preferred position are you issuing them at? Are you issuing them at the market level or are you issuing them so that the shareholders will get a capital gain immediately they are taken up?

Mr. PATON: Under the act under which we are operating at the present time, there is a limitation on the price at which we can offer shares. We cannot offer them in excess of the capital and rest account of the bank. Perhaps to give you an instance of the bank that you and I are fairly well acquainted with, the Toronto-Dominion Bank's capital and rest account as at December 1965 was \$126 million; our capitalization is 3 million shares and, therefore, the maximum price that we could issue shares under the current act that we have would be \$42 per share, if my mathematics are right. The present market is in the neighbourhood of \$57. Under the new act this limitation on the amount at which shares can be issued will be removed and it will then be a matter of management judgment if, indeed, they decide to issue shares, as to what price the shares would be issued at.

Mr. LIND: There is no more control under the new act?

Mr. PATON: Under the new act that is the situation. Mr. Elderkin, am I correct in that, sir?

Mr. ELDERKIN: That is right.

*(Translation)*

Mr. CLERMONT: If you will allow me, I would like to come back to the document—

*(English)*

The CHAIRMAN: Oh, I am sorry; perhaps I have made a mistake. I had the impression that Mr. Johnston was through with questioning and that it was Mr. Clermont's turn to follow you.

Mr. JOHNSTON: No, I was not finished, sir. I trust I have some time left.

The CHAIRMAN: Yes. I apologize to you both. It was my error in this regard.

Mr. JOHNSTON: Is your profit position satisfactory until you start comparing it with the near-banks?

Mr. PATON: A profit situation can always be improved, Mr. Johnston; that is management's incentive to operate, and I hope that we always will operate under

an economy that will permit this. It would be incorrect to say that profits level are satisfactory from any basis. We would like to see, through more efficient operation, if we can improve our earnings. If you relate our profits to our assets, and to our capital, the earnings picture is not what we would consider at a completely satisfactory level.

The CHAIRMAN: Mr. Johnston, I think that I have made another error in the last few minutes in that I may have permitted a question which may be considered somewhat remote from our topic, which is the recommendation of the government that the interest rate ceiling be changed from what it is. Now you may feel that the questions have been related to this topic. It has just occurred to me, and I accept responsibility for the error in not noting this possible movement away from the path we are following. I should draw this to your attention.

Mr. JOHNSTON: Well, I felt the question had a great deal to do with the topic. Really what I am striving for is some reason for the increase, and if we more or less accept the statement of the bank, the reason becomes sort of a charitable one. But if we look at the profit question then we shift the balance again.

Mr. CHAIRMAN: That is fine; you have related your question to the interest rate.

Mr. JOHNSTON: If I look at schedule A, the return on shareholders equity. And if we think in terms of the sort of comparative view of it, it would seem to me that finance companies, in the ten years, have had a rather disastrous decline in return on shareholders' equity, from \$15.10 to low of \$9.30, and a bit of a recovery in 1964. On the other hand, if one looks at the return on shareholders equity for the chartered bank, we seem to have a long process of almost consistent improvement on the return. Now in view of all we have heard about the difficulties of competing with the finance companies, trust companies, the figures here seemed a bit surprising to me. I was wondering if there was any simple explanation for them.

Mr. PATON: I do not think that I can read much more into these figures, Mr. Johnston, than I have shown. Obviously notwithstanding the drastic reduction referred to, the finance companies will still on the average have 10.80 as contrasted to the chartered banks 7.14. So that notwithstanding this reduction there is still approximately a 50 per cent differential.

Mr. JOHNSTON: So if you took a long range view it might be better to invest in a chartered bank than in a finance company, as these approach the point where they intersect. On top of the declared revenues I understand there are hidden reserves. Do the banks pay taxation on the accumulated earnings of these hidden reserves?

Mr. PATON: I would like to correct the word "hidden"; they are "inner" reserves.

Mr. JOHNSTON: Inner reserves.

Mr. PATON: They are not hidden in that they are fully disclosed to the authorities as prescribed in the Bank Act. These reserves are non-taxed when they are put into inner reserves under the specified formula prescribed by the authorities.

The CHAIRMAN: I would suggest, Mr. Johnston, there is a section in the bankers' brief on this inner reserve question, and if we work on the line of procedure we have agreed on, we should have a series of rounds on the question of the reserves.

Mr. JOHNSTON: Mr. Chairman, I have only one or two more questions. Rather than increasing the rate via the chartered banks, would it not be a better solution to limit the interest rate that can be charged by the near-banks, and to narrow the gap?

Mr. PATON: I think not. I think the basic philosophy of the banks' position is open competition. If we endeavour to inhibit others to bring a more unified approach, we are going about it the wrong way in my view.

Mr. JOHNSTON: In other words you are not criticizing the freedom of the others; you are criticizing the restrictions on the banks.

Mr. PATON: We would like to see ourselves free to compete.

Mr. JOHNSTON: If you limited the whole thing then we would run into a problem. Have you any guide or measure as to what constitutes an exorbitant rate of interest?

Mr. PATON: I have never participated in that area at all, so I do not think I am qualified to answer that question.

The CHAIRMAN: Have you not observed the activities of others?

*(Translation)*

And now Mr. Clermont.

Mr. CLERMONT: Mr. Chairman, may I be allowed to revert to the report submitted to the Committee, with regard more particularly to consumer loans and to the example given there of a \$1000 loan? Mr. Dixon, in answer to a supplementary answer of mine, explained that the differences there came because in one month there could be 30 or 31 days. To me that is not a satisfactory answer. The report, as it happens, deals with eight banks. Now in six cases similar figures are given for \$1000 loans over thirty-six months. In that instance I will of course accept Mr. Dixon's answer. Still I note that in the case of Bank "A", on a \$1000 loan repayable over thirty-six months, the interest of discount rate indicated is \$92.40 whereas in the case of another bank, which I will call Bank "G" it is \$98.62, which is a seven dollar difference. In the case of the six other banks Mr. Dixon's answer is obviously the right one, since the difference is only about 50 cents, not even one dollar.

*(English)*

Mr. DIXON: I can only say in answer to the questions that these are the interest calculations that were made by each one of the individual banks, and perhaps the bank that feels it has made an error will correct it. I really cannot account for it sir. These are the figures that they gave to me.

*(Translation)*

Mr. CLERMONT: We will have to put these questions to the Bankers' Association because here we are working with letters, and we don't know what banks are being dealt with.

Mr. LAVOIE: Mr. Clermont, if you will allow me. We are going to have a meeting of the Association and this is a question I would like to discuss there. We



might be able to answer your question then. I think it is a very proper question as there is indeed a considerable difference between the amount charged by one bank, that is \$99.40 for thirty-six months and another \$92.00.

Mr. CLERMONT: At this meeting, could you also ask explanations for bank "E" which makes no distinction between interest and discount and service charges? Because, for the thirty-six months they show an amount of \$174.85 which is, I think, the highest combined rate of all banks.

Mr. LAVOIE: The bank in question has not changed the system that it has had over the years. This is a question which was discussed at a meeting on the Bank Act in 1954 at which the representative of that bank gave us an explanation about these rates. I think that if you require additional explanations Mr. Clermont, we will give them to you.

Mr. CLERMONT: I don't think the word would be "require", but I think that it would be of interest to the Committee to receive explanations in this connection, because it seems to me that this is the bank that has the highest combined interest and service charge.

Mr. LAVOIE: For thirty-six months?

Mr. CLERMONT: Not for twelve or the twenty-four months, but for thirty-six months.

Mr. LAVOIE: We will give you that answer, Mr. Clermont.

Mr. CLERMONT: Mr. Chairman, with regard to service charges, I think that if you have a look at Section 93 of the present Act, you will see that it states that "no bank shall directly or indirectly charge or receive any sum for the keeping of an account unless the charge is made by express agreement between the bank and the customer".

Mr. LAVOIE: Yes, this is correct.

Mr. CLERMONT: Which means that when a person opens a bank account he signs a form or forms?

Mr. LAVOIE: Yes, Mr. Clermont.

Mr. CLERMONT: Would it be possible, Mr. Chairman, for these forms or specimen forms to be tabled before this Committee?

The CHAIRMAN: Yes, this could be done. If you will put up a proper request I will see to it that these forms be procured.

Mr. CLERMONT: A copy of the forms that people sign when they go to a bank to open a savings or a current account should be tabled before the Committee.

Mr. LAVOIE: The bank account and the forms that are required particularly for the Provincial Bank with regard to the service charges and others? Yes, we will procure these for you. The forms vary from one bank to another, however.

Mr. CLERMONT: That is why I mentioned the Provincial Bank or the Banque Canadienne Nationale, that is Form 31 and Form 16.

Mr. LAVOIE: You have a very good memory, sir.

Mr. CLERMONT: Is the Committee in agreement?

The CHAIRMAN: Yes, you can ask this, and as Chairman I will ask our witnesses to give us this. Clause 96 (3).

Mr. CLERMONT: Mr. Chairman, I think my request is not only with regard to the Provincial Bank of Canada, but to all chartered banks. Mr. Chairman, this question could be directed either to Mr. Paton or to Mr. Lavoie. If a customer, or a potential customer, refused to sign these forms would his deposit be refused or accepted nevertheless?

Mr. LAVOIE: I think banks have the privilege of accepting or refusing any deposit that a customer might want to make. For instance if someone goes to a bank and wants to deposit a cheque, and we are not sure of the value of this cheque, we could refuse to open the account even in these circumstances.

Mr. CLERMONT: Mr. Chairman, could I ask Mr. Paton and Mr. Lavoie again if they are aware of the service charge in the United States in regard to cheques on savings or current accounts?

Mr. LAVOIE: In the United States, I am told that there are no cheques drawn on savings accounts.

Mr. CLERMONT: I know. How about current accounts?

Mr. LAVOIE: They have the privilege of issuing cheques on current accounts. I do not think I have this information.

The CHAIRMAN: We will obtain this information for you and present it. I have asked the gentleman to make an inquiry in this respect, and to answer Mr. Clermont.

Mr. CLERMONT: Now I would like to revert to another brief: the report of the Canadian Bankers' Association tabled before this Committee and entitled "Some Reflections on the Profitability of the Banking System in Canada". Representatives of the Canadian Bankers' Association at different times have indicated that they would like the interest ceiling to disappear to allow for more extensive opportunity. They gave us this report. On table C we have a comparison of 20 American companies including American commercial banks. In the United States there are no interest ceilings. According to that table, Mr. Chairman, I notice that the yield of commercial banks is 8.8 and it is the second lowest of the 20 companies. The lowest is a real estate, but you have the same situation with regard to banks in Canada. In the list you provided for us in Table A, banks are quoted at 7.49 the lowest being 4.02, you claim however that removing the ceiling would give you more opportunity to increase the yield per shareholder.

Mr. LAVOIE: We are looking at the tables you mentioned, and on E you have the yield for chartered banks. In Canada the average for the last 5 years is 7.14 and for the eleven years from 1945 to 1957, 6.79. In the United States the yield is 8.8 or 9.

Mr. CLERMONT: But I am comparing these figures with those of other American corporations whereas you make the same comparison with Canadian corporations in Table A—

Mr. LAVOIE: But if you look at Table 3 you will also see wide variations from year to year. In manufacturing for instance, we have a high of 15 per cent and lows of 10 and 9.8. In trade you have less important variations. In the finance company area—which is most like banking—you have a yield of 16.4 to 12 per cent.

Mr. CLERMONT: I do not think I quite get my point over. If the interest rate ceiling disappeared would your position with regard to yield improve in comparison with other Canadian companies?

Mr. LAVOIE: This is hard to say. If the ceiling were removed and if chartered banks increased their rate of interest on savings, there would be a certain offset which would be set up between the two, and it might not increase the income of the banks.

Mr. CLERMONT: Mr. Chairman, on their deposits in the Bank of Canada, do chartered banks receive, in interest over one billion, for instance.

Mr. LAVOIE: Chartered banks have to maintain a reserve of 8 per cent without interest in the Bank of Canada.

Mr. CLERMONT: What do you mean by your expression in your report of 24th October, your brief which came to the Committee. Not the one Mr. Payton read to this Committee but the one that we received. That we the members of this Committee, dated 24th October.

Mr. LAVOIE: Page 8, I believe.

Mr. CLERMONT: The French version chartered banks and I quote "do not cash any in excess amount".

Mr. LAVOIE: I think this is a question of translation. We translate that from English to French. As the chartered banks do not have any interest on their deposits of the Central Bank, we might say that it is "higher than one billion".

Mr. CLERMONT: It is not quite the same thing.

Mr. LAVOIE: No, it is not.

(English)

The CHAIRMAN: Now, I recognize Mr. Lambert.

Mr. LAMBERT: First of all, following up on Mr. Clermont's questions on the brief submitted by the C.B.A. schedules A and C. This is in the profitability brief—is it understood that the term "return on shareholders equity" and "rate of return of net worth" are exactly interchangeable terms? What I want to make sure of, Mr. Chairman, is that when we are speaking of a comparison between schedules A and C in this brief that we are speaking of percentages of the same thing, not percentages of apples and oranges.

The CHAIRMAN: I think that is a valuable point. Perhaps this is a matter of accounting terminology, which is a difficult area at any time.

Mr. LAMBERT: I think the burden is on the C.B.A. to say: "That is all right; fine." Just to clear up that point.

Mr. COLEMAN: The net worth of a company is the equity in the company owned by the shareholders. It is a very good point, Mr. Lambert.

Mr. LAMBERT: Now, continuing a supplementary that Dr. McLean had gone into, in so far as any variation in the interest chargeable to the customers is concerned, is it not a fact that prior to the market rate going up to the ceiling of 6 percent you did have a prime rate and therefore the risk assessment of varying customers could vary on the basis of the prime rate up to 6 per cent?



What you now want is again the operation of a prime rate based upon the market which you cannot have at the present time?

Mr. PATON: That is correct.

Mr. LAMBERT: Let me revert back to the point I tried to make the other day in connection with clause 91 and the exemptions to the ceiling on interest as provided by subclause (6). I think we were having a little difficulty getting an answer from Mr. Paton. Assuming the 7 per cent ceiling on the interest rate as set by clause 91 conceivably can continue for the lifetime of this present act, do the exemptions or exceptions granted under subclause (6) provide a meaningful field of operations for the chartered banks, or is it merely a question of saying, yes, 95 per cent of your business will be controlled by the fixed ceiling interest rate with only 5 per cent uncontrolled? After all, your essential brief has been to take the ceiling off. The Porter Commission report said: Take the ceiling off in order to create more competition. Is this provision in this act meaningful, in the opinion of the Canadian Bankers' Association?

Mr. PATON: I think the short answer to your question, Mr. Lambert, is that it is not as meaningful as we would like. Under present monetary conditions, with the available funds we have, we are inadequately looking after the demands from our borrowers at the present time. There is a form of rationing in our lending ability now. The sudden change from 6 per cent ceiling to 7 per cent or  $7\frac{1}{4}$  per cent will ease this situation and, to some extent, undoubtedly will permit us to participate in these other areas. But to say that it would do so in a really meaningful manner would be, certainly in the short term run, exaggerated.

Mr. LAMBERT: May I try to get a further particularization on this. Is it at all possible to determine a percentage of your mix of loaning business which might come under the exceptions granted in subclause (6). Is it 25 percent? When I ask you, is it meaningful within your business, surely to come to a conclusion of yes or no you must, in your mind, say, well maybe we can do 40 per cent of our business or, it is only 10 per cent. So then you can answer by a yes or no: Is it meaningful?

Mr. PATON: Perhaps it would help if I used the analogy of our participation in the N.H.A. field. In 1954, as you are aware, the chartered banks were permitted entry into that lending field. I think, in round figures, we possibly reached somewhere in the neighbourhood of 7 to 8 per cent of our assets which were invested in N.H.A. mortgages. I may be out somewhat but it was fairly close to that figure. Currently, we have, I think, about \$800 million in N.H.A. mortgages and our total banking assets are in the neighbourhood of \$26 billion. So roughly 3 per cent is outstanding at the present time in the specialized lending field that is presently permitted to us. I would say if we were to look forward to a similar 3 per cent this would not be meaningful in our interpretation of "meaningful". But, I do not think that any of us can put up a yardstick presently on this question simply because of the fact that there is an unsatisfied demand for loans currently which, assuming we were able to put our hands on those funds, we would be called upon to meet. These are the loans that we are making to finance the commerce and industry of the country. Part of it would come into this picture—perhaps one of the others might be prepared to put a figure on it. But we have examined the situation very closely: we have endeavoured to project an allocation that we would put into N.H.A. and conventional

mortgages into industrial financing, capital financing of business, thereby enabling us to be of greater help to them in their operations. At the present time we have not come up with any figure.

Mr. LAMBERT: Is the proposed clause 91 something under which the banks could live with satisfactory freedom in the light of their representations, your brief, plus the recommendations of the Porter Commission with regard to greater competition. If you cannot do it, in what sectors would you want an enlargement?

Mr. PATON: We would like complete removal of the ceiling. That is the approach we have in our brief; that is the final message on this subject, on this particular part of our brief, that we would like to leave with the committee. We feel that complete removal of the interest rate ceiling is in the interest of the Canadian economy. This would enable us to participate in a meaningful manner in the additional forms of lending that we would be privileged to undertake under Bill No. C-222.

Mr. LAMBERT: I do not think that you are taking so inflexible a position, Mr. Paton, in this regard that you would be like some lawyers who might be quite prepared to settle at all times for 100 per cent of claim and costs.

Mr. PATON: Having made my point; I would say that certainly any amelioration of this interest rate ceiling would be helpful. But I was endeavouring to put a yardstick on the word "meaningful". I cannot see that there would be in the short run a sudden and substantial influx of banking funds into this area based on a 7 or  $7\frac{1}{4}$  per cent ceiling rate.

Mr. LAMBERT: We have four primary or indicated exceptions under subclause (6). If it is not meaningful perhaps it might be more meaningful if you could suggest one or two other categories within that subclause. After all, what I am trying to do, perhaps, is say all right, where is an area of negotiation or of compromise in this regard. I hope the bankers association are not taking the position it is all our claim or nothing.

Mr. PATON: I do not think we have that in our brief, Mr. Lambert.

Mr. LAMBERT: No, I am not suggesting you have but I would not want that interpretation. I would like to have some assistance in seeing if there is another area on which, perhaps, members of the committee might suggest to the government, that the bill should be amended.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I think, Mr. Chairman, I take strong exception to Mr. Lambert's suggestion that we are engaged in some sort of negotiations with the banks because we are not. We are legislators. We shall legislate in the interests of the Canadian people. The banks will damn well have to accommodate themselves to it. This is the position, and I do not think they should be encouraged to think that they can bargain.

Mr. LAMBERT: I am not suggesting bargaining; I am interested Mr. Cameron, in trying to improve the legislation to make it more workable.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You were speaking in terms of negotiation and bargaining.

The CHAIRMAN: I think, gentlemen, Mr. Lambert may have created the impression because he used the analogy of a lawyer negotiating a settlement.

Perhaps if we take his remarks in the spirit of inviting the witnesses to make suggestions on which we may or may not base our legislation, we can all be in agreement on the concepts involved.

Mr. PATON: Mr. Lambert has an unanswered question regarding other areas.

Mr. LAMBERT: That is right. Are there any areas beyond the four indicated in (6) (a), (b), (c) and (d) which would make the legislation much more meaningful?

Mr. PATON: If you would like me to endeavour to answer that, Mr. Lambert, there is one limitation in these special lending areas, namely the 75 per cent, on conventional residential mortgages. Insofar as the rate of growth at which banks can participate is concerned, I think in general these areas cover quite substantially the various fields in which the banks feel they could be of assistance in the Canadian economy. Our aims and ambitions are not so far removed from Mr. Cameron's as a legislator. We have the interest of the Canadian public as our primary concern because automatically this is in our own interest. I would suggest, as I did last week, perhaps, an area that could be considered as falling short of the full 100 per cent discussed, that the trigger rate of  $4\frac{1}{2}$  per cent, conceivably, could be set at perhaps 5 per cent, which would under conditions as we see them, perhaps allow the complete removal of the ceiling closer to the time anticipated at the time this legislation came down. I think it was mentioned in *Hansard*, that in possibly one or two years this ceiling would be removed. As our brief points out, this becomes somewhat further in the future as current conditions continue.

Alternatively, we have suggested we have a time limit set for the removal of the ceiling say, perhaps one or two years following the passage of this bill, thereby cushioning what I think the minister suggested might be a shock—I think that is one of the words he used, or one of the members used—caused by the ceiling removal. I think that would be two possibilities that would be of interest to the association.

Mr. LAMBERT: Fine. That completes my question at this time.

The CHAIRMAN: I think Mr. Laflamme has a supplementary question.

Mr. LAFLAMME: Mr. Paton, I would like to know more precisely what more can you do if the 6 per cent interest rate was completely removed for the Canadian public.

The CHAIRMAN: You mean right now, in the short run?

Mr. LAFLAMME: Yes. You said that it would be in the interests of the Canadian public, but that is a very broad answer.

Mr. PATON: I think possibly the Porter Commission put it better than I can, Mr. Laflamme in their report regarding the recommendation that the 6 per cent be completely removed. We are, have been, and hope to continue to be, the main financial institutions in financing Canada's economy from coast to coast, and release from these inhibitions we are currently operating under would enable us to perform this function much more efficiently and much more satisfactorily for the Canadian public. Our primary concern at all times has been the public, sir, because I think it is automatic in any profit-earning operation. If the public benefits then it benefits the bank. Our concern, as I have mentioned earlier, is not



with the sudden influx or large increase in our earnings, although we are and consistently are very conscious of our shareholders interests. Our concern is to get this banking operation functioning at its most efficient standard. With these limitations under the present act we cannot do so.

Mr. McLEAN (*Charlotte*): May I ask a supplementary, Mr. Chairman? If the rate jumps to  $7\frac{1}{4}$  per cent under the proposed act does this become a maximum or a minimum rate? Does it stop the idea of having any prime rates?

Mr. PATON: No sir. If the rate was  $7\frac{1}{4}$  I would say there would be a prime rate under  $7\frac{1}{4}$  per cent.

Mr. McLEAN (*Charlotte*): Then it would be a maximum.

Mr. PATON: That would be a maximum but we would be getting back to a range that would be considerably narrower than we should normally operate under.

The CHAIRMAN: I suggest, Mr. Lind, that you begin your questioning, and in view of the committee recessing at about five to one, you could continue your questioning after we resume this afternoon.

Mr. LIND: Thank you very much, Mr. Chairman. I would like to go to the brief here, with some brief comments on the profitability of the Canadian banking industry. I would like to read first: Evidence already placed before you by the Governor of the Bank of Canada has indicated the more rapid growth of the near-banks during the past decade in comparison with the chartered banks. I would like to relate this to competition and interest rates. I will tie in interest rates.

The CHAIRMAN: This is the area we are discussing.

Mr. LIND: Mr. Paton, your association seems to be always attacking the position of the near-banks. Are you not trying to eliminate competition between yourselves and them?

Mr. PATON: No sir.

Mr. LIND: Not in the least?

Mr. PATON: This has never entered our minds in any of the presentations we have made before the Porter Commission and in our brief here, sir—and I hope in our verbal presentation too. We think there is a place for near-banks or, as the governor, I think, referred to them, non-bank financial institutions. Certainly there is a place for them. We have no thought in our mind that we would eliminate them.

Mr. LIND: Then you would adhere totally to this concluding paragraph in the Porter Commission report at page 375:

—we recommend that the powers of the banking institutions be broader than any of them exercises under present legislation. They should all be free to invest in N.H.A. or in conventional mortgages, subject in their conventional lending to the 75 per cent loan to value limit recommended in Chapter 14. Similarly, they should all be free to make commercial and personal loans without restriction on the security they choose to take, and

should all be entitled to the classes of security now available to chartered banks under Section 88 and related parts of the Bank Act, and to any loan guarantees which are offered by the government to the present chartered banks. Other institutions need the same access to security as chartered banks if they are to compete effectively in this area, particularly as the banks long experience and established position will give them a great working advantage.

Do you adhere wholeheartedly, to that conclusion of the Porter commission?

Mr. PATON: If these prerogatives were given to the near-banks, Mr. Lind, they would then be operating as banks. We have never, at any time, endeavoured to stifle competition. In fact, we have stated that we are quite in favour of competition, and we would not quarrel with that statement made by the Porter commission. We have not asked for preferences; we have asked for the removal of limitations we currently have. If we are consistent in that view, then we should be in accord with the gist of what you read.

Mr. LIND: Would you be prepared to go one step further and allow them to be known as banks or banking institutions?

The CHAIRMAN: Mr. Lind, the question is certainly relevant to our total responsibility, but you should relate this to the question of interest rates. Otherwise, I might ask you to hold this off until a later phase.

Mr. LIND: I am trying to relate it to the interest rates paid on deposits.

The CHAIRMAN: In that case, you can answer the question, Mr. Paton.

Mr. PATON: Was your point whether we would object to their being known as banks? If so, provided they met all the requirements of a bank, there is no reason why they should not be known as banks. But they must meet the legal requirements and operate under the same ground rules.

Mr. LIND: Do the Canadian banks operate on the same ground rules as the United States banks, where there seems to be more competition?

Mr. PATON: I would question the accuracy of your premise. I do not think there is more competition in the United States than there is in Canada. In fact, I would use a stronger word than "think".

Mr. LIND: Now I am going to relate this to the interest. The Canadian banks continue to pay three per cent on savings deposits. Is that not right?

Mr. PATON: Yes.

Mr. LIND: And the American banks are paying approximately five per cent on savings deposits at the present time.

Mr. PATON: These are quite different savings deposits, Mr. Lind. Canadian banks are paying a rate of interest in excess of five per cent on savings certificates and special types of savings. These are pure savings, per periods of say six months, a year or five years. On the savings on which cheques are permitted in Canada—which is a unique situation, as you are well aware—the going rate is three per cent per annum on the minimum quarterly balance.

Mr. LIND: On the minimum quarterly balance.

The CHAIRMAN: Mr. Lind, you seem to be entering into a very interesting line of enquiry and, rather than interrupt you, I suggest that we recess at this point and resume at 3.45 p.m. You will be the first speaker at that time.

#### AFTERNOON SITTING

*(Recorded by Electronic Apparatus)*

The CHAIRMAN: Gentlemen, I would like to resume the meeting. It will be on an unofficial basis with the usual reservations at this point. When we recessed I believe that Mr. Lind had the floor.

Mr. LIND: Thank you, Mr. Chairman. I think we were discussing when we recessed the comparison between the interest rate paid on deposits in Canada and the interest rate paid on deposits in the U.S.A., which is roughly 2 per cent more. The next question I would like to ask Mr. Paton is: do they anticipate raising the interest rate on deposits so it will help out the small depositor across Canada as a whole?

Mr. PATON: Your question is presupposing that the interest ceiling is removed or is changed?

Mr. LIND: Yes, in some method.

Mr. PATON: I would say that would be a logical expectation, that there would be some effort made. There would be a change made in the treatment of our savings depositors and this might take the form of perhaps a different type of savings account or a different type of certificate, but the savings depositor would benefit.

Mr. LIND: Let us go back to the area of loans. I think there was a statement made this morning by Mr. Coleman that all loans are not secured loans. Do you loan money without a personal guarantee if you do not get security for it?

Mr. PATON: Yes, sir. That is a very common method of banking, banking against a statement of position.

The CHAIRMAN: Do you have a note signed?

Mr. PATON: Oh, yes, we have a promissory note. Evidence of the debt is signed. Mr. Lind, I think you were referring to a specific guarantee behind this note.

The CHAIRMAN: You do not consider a note as a form of security?

Mr. PATON: Mr. Gray, it is a form of debt. It is an unsecured charge against the asset by itself, against the borrower's worth. If there is an outside guarantee, somebody independent of the borrower maybe is providing the security.

Mr. LIND: If this interest ceiling is lifted, is it the banks' intention to enter as aggressively into the N.H.A. mortgage field as they did after 1954?

Mr. PATON: I think we should say that our experience in the relatively short time we were able to participate in that area of lending is sufficiently encouraging that we would certainly look on it favourably to the maximum extent of our resources.



Mr. LIND: I think I made an error. I think it should be the 1957-59 period, when you went into it to the extent of about 60 per cent of the N.H.A. loans at that time?

Mr. PATON: Yes. We started getting into it in 1954, and I think it was around 1959 that we were excluded from participating due to the ceiling rate.

Mr. LIND: What I am concerned about is the small areas throughout the country where banks have branches. Will your managers be encouraged, if this ceiling should be lifted, to go into the N.H.A. lending field in these rural areas again?

Mr. PATON: We are admirably situated to do just this, and this would be the intent in areas where other lenders are possibly not in at the present time.

Mr. LIND: Now, there is one area here this morning in your brief where you point out the comparison between the various institutions, and I imagine you take your coinage and paper as inventory, do you, or what do you take as inventory in a bank?

Mr. CAMERON: Brains.

Mr. PATON: Mr. Cameron has just answered the question, Mr. Lind.

Mr. LIND: You said brains as inventory.

Mr. PATON: We have some brawn, too.

Mr. LIND: Well, you must have some commodity to do business with. What commodity is it? Just paper and coinage? Is that what it is?

Mr. PATON: Our working tools are our till money, our paper and our coin and, of course, our credit facilities also.

Mr. LIND: Is there much obsolescence in this?

Mr. PATON: No, sir, not too great.

Mr. LIND: You would not consider your loss factor then on inventory as great as in the construction business?

Mr. PATON: In our real inventory, yes. Inventory is your earning asset. It is the same as in the construction and manufacturing business, certainly we have losses in our earning assets. Our earning assets are our loans, our investments and all assets that produce revenue to the bank. This is the area in which our losses occur. Any losses we have in our till money are generally due to circumstances beyond our control.

Mr. LIND: But is that not chargeable back?

Mr. PATON: If we can find them.

Mr. LIND: You would admit that your inventory loss probably would not be as heavy as it is in the construction business.

Mr. PATON: Well, I think I might even dispute that, Mr. Lind, to some extent. As we said in our brief, a relatively small loss percentagewise can make considerable inroads into our income revenue for year. We pointed out that roughly a one per cent loss would account for almost our earnings for year.

The CHAIRMAN: At this time I will ask for a motion to make our proceedings official and have them officially incorporated.

Mr. MORE (*Regina City*): I so move.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I second the motion.

Motion agreed to.

Mr. PATON: On page 13 at the second paragraph we refer to losses:

Because of the overwhelming size of their liabilities and assets in relation to the income of any one year a very small percentage loss on assets—less than one per cent—would completely wipe out the year's income of any Canadian bank, producing an over-all net deficit.

Mr. LIND: Pardon me, Mr. Chairman. What page is that on?

Mr. PATON: Page 13 of our brief.

Mr. LIND: What I was coming to, Mr. Paton, is that in manufacturing we have loss due to loss of inventory, obsolete inventory construction and all these other trades, and I was just wondering if your percentage of loss was as great as some areas in some other lines of construction, manufacturing and retailing and so on.

The CHAIRMAN: The percentage of assets?

Mr. LIND: Inventory losses. You did not give me the actual figure on that, although it is something less than one per cent.

Mr. PATON: I have some statistics here, which deal with a number of years, Mr. Lind, that I might quote to you. In 1956, for example, the loss experience of the banks as a percentage to eligible assets, which include investments as well as loans was 1.20 per cent. Translated into a percentage of the earnings of that specific year it represented 97 per cent.

Mr. LIND: That does not mean much to me because I did not know the bank assets of that year. If you would put that as a dollar figure I could maybe understand it.

Mr. PATON: I have them as percentages. It shows the relationship of losses to earnings for one year, which points up the necessity for us to provide for such losses by being permitted to carry reserves.

Mr. LIND: In those losses what would you include?

Mr. PATON: These are losses in relation of loans and certain investments, i.e. eligible risks assets as defined by the authority of the Bank Act and are losses attributed entirely to judgments or decisions that did not prove out correct.

Mr. LIND: Yes, but would you not also have a compensating balance there, where the judgment was good, and you had the capital gains to balance against this, the securities, bonds and what-not?

Mr. PATON: Income from our bonds is part of our income for the year. The income from these bonds and securities of a similar nature would be in our revenue.

Mr. LIND: You are talking about losses to the trade in your commercial accounts.

Mr. PATON: That is the major item.

Mr. LIND: Where would you find the major loss of this, in the consumer field or in the commercial field?

Mr. PATON: This is one subject on which each bank would have a different experience. In general, the losses would be across the lending field in which the banks engage. In all probability, each bank would have a different experience in certain areas than others would. Each one of them, I assume, would know in which area their own loss experience had been.

Mr. LIND: Would it be safe to assume that your loss figures would be greater in the consumer lending field than in the commercial lending field?

Mr. PATON: On a percentage basis in relation to the total outstanding I would say that possibly that is so. It is a higher risk area than some others. I think I heard a "No" from one of my colleagues down on the far right-hand side. This would be my opinion, but I am not quite sure if this would be yours, Mr. Coleman.

Mr. COLEMAN: With respect, Mr. Paton, I would not think that that is right. Although I do not have the information right at hand, I think the banks' experience in the consumer loan business has been good, and I think that the ratio of losses has compared favourably with other lending institutions. I would think that relatively and in dollars that the losses in commercial accounts would be substantially greater than in consumer loans. You might lose as much in one large commercial account as you would lose for perhaps a couple of years in consumer loans.

Mr. LIND: But you amortize that over a two or three year period. Do you not build reserves for that?

Mr. COLEMAN: But it is still a loss.

Mr. LIND: Now did the banks enter the consumer market first in 1954?

Mr. PATON: The 1954 revision facilitated the entry of the banks into consumer lending, generally, in the form of enabling us to take security in personal property.

Mr. LIND: I have a figure here so I might as well tell you my source; it is the Bank of Canada statistical summary for October 1966. Consumer lending by the banks increased from \$351 million in 1954 to 2 billion, 331 million dollars in June 1966, where they have taken their share of 33 per cent of the consumer market. Now, what I was interested in, and you have practically answered my question, is that you say your loss in the consumer market is less than in the commercial or in the industrial end of it.

Mr. PATON: I would not want to present myself as being a better commercial lender than my colleagues here, but I would still like to reserve my agreement on that figure until I examine it to my own satisfaction, so far as losses are concerned. However, on the assumption of Mr. Coleman's reply, which I think would be the consensus of the association, I will go along with that.

Mr. LIND: There is no doubt in the consumer market that the banks are expanding very rapidly. If the interest rate is raised from six per cent to



whatever we raise it up to, and you have a little more interest, they can take a little more risk. Will you endeavour to service more consumer loans across Canada?

Mr. PATON: Yes, I would say that that would be our general endeavour.

Mr. LIND: In other words, we would expect then that more people in Canada will benefit if the interest rate is raised so that the banks can cover more people or, to put it another way, you can step down one category and take on more risks in consumer credit.

Mr. PATON: We like to look on it as an element of greater risk rather than refer to it as being risky.

The CHAIRMAN: I think you gentlemen invited this by your reference to commodities this morning.

Mr. LIND: I am personally concerned as to whether the chartered banks are going to offer to more people in Canada consumer financing than they are at the present time. At the present time they have 33 per cent of the business. Are they going to try to increase that to 50 per cent so that more of our people will have a chance to take advantage of, shall we say, this preferred rate of consumer financing.

Mr. PATON: Mr. Lind, I would say yes without specifying percentages. We feel that our entry into this field has benefited Canadians through bringing the cost of consumer financing down to the borrower, and in the continuation of that procedure we would take full advantage, to the best of our ability, to expand it.

The CHAIRMAN: Do you have a supplementary?

Mr. LAFLAMME: Only if you receive more deposits.

Mr. PATON: Correct. I said to the best of our ability.

Mr. LAFLAMME: What will you do to attract more deposits? Will you increase your interest on the deposits?

Mr. PATON: I think I answered that point. Our intention would be that our depositors would benefit by enabling us to attract more deposits to service a greater loaning total.

The CHAIRMAN: Mr. Lind, your 20 minutes seems to have passed by.

Mr. LIND: I have one more question.

Mr. CLERMONT: I have a supplementary.

The CHAIRMAN: I will accept your supplementary after Mr. Lind's question.

Mr. LIND: Will every branch of your banks all over Canada be authorized to issue consumer credits so that all people across Canada will benefit from this lower consumer rate?

Mr. PATON: They are now and they will continue to do so.

(Translation)

The CHAIRMAN: Will you ask your question now, Mr. Clermont?

Mr. CLERMONT: This is with respect to a question Mr. Lind asked you regarding consumer loans. If parliament abolished the ceiling rate on loans, will the banks take into consideration reducing their service charges, because if they

increase their interest rate, plus the regular charges they charge today the consumer loan—instead of being between 10 or 12 per cent will be between 14 and 15 per cent, which will approach maybe the rate by other financial institutions.

(English)

Mr. PATON: Any alleviation on the interest rate, Mr. Clermont, would not have a direct connection with any service charge we currently are assessing. The service charge would be a matter of us operating as efficiently as we can but yet bringing our services to the Canadian public as cheaply as we can—and believe me, they do get them cheaply in relation to many other countries. If we do that, the service charges might well be reduced through a more efficient operation as we progress from time to time. But the direct relationship would not be there.

Mr. CLERMONT: Thank you, Mr. Chairman.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I would like to pursue this question a little further. I have found some difficulty in grasping the concept of the cost of money, and possibly my brain has become a little obsolescent. When you speak of the cost of money—and I am now thinking of the cost of money to the banks—would this include the interest paid to your depositors, the labour costs of operating the account and the general overhead costs of the bank itself? Would that be the cost of money to you?

Mr. PATON: No, Mr. Cameron. My conception—and once again I will probably have Mr. Coleman supplement my answer—of the cost of money is a direct cost, as a manufacturer has a direct cost. This is a direct cost, what it costs me to gather that money into my bank.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then you would include in your cost of money merely the interest paid on the deposits?

Mr. PATON: Just whatever it costs me—if I have to pay, for example, a finder's fee, this would all go into the actual cost of money which I have to pay. That would be my direct cost and on that cost I would relate my interest charge. All the other concomitant costs of operating a loan account of a borrower would be tied up in the substantial supervision that is required to ensure that the individual's or the company's affairs are followed and that the loan continues to be a good loan.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I am still rather at a loss to understand what distinction you make between these costs. I recall in 1954, at the hearings at that time, if I remember correctly, there was only one bank which was at that time making personal loans with service charges that equalled the interest charge. I think the average worked out to about 10½ per cent altogether. They were stated in terms of 6 per cent interest rate and 6 per cent service charge. You may recall that at that time there appeared to be conflicting legal opinion. The general manager of the Bank of Commerce, which was the bank engaged in this, said their legal opinion was that this was not a contravention of the Bank Act. Representatives of the other banks had some doubts about the legality of this and they claimed they had legal opinion that it was a contravention of the Bank Act.

I would imagine that the opinions which said it was a contravention of the Bank Act considered that this was an evasion of the ceiling on interest rates,

camouflaged as service charges. One can only assume that was the basis of the legal opinion which apparently had been tendered to all the banks except the Bank of Commerce. How has that situation changed from that time until now? Have you had different legal opinions since then?

Mr. PATON: We all have had—and I think I would be covering all the banks, Mr. Cameron—legal opinion regarding the manner in which we are operating our consumer loan plans. Our personal loan plans are strictly legal.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): There has been a change of general legal opinions then, in the past 12 years?

Mr. PATON: I would assume so, yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): May I now come to the question of the interest charge itself? I presume that the interest charge that you make includes, as the number one item, and quite rightly, your profit on operations. In addition to that, would there not be some other costs that would be considered in setting your interest rate?

Mr. PATON: You are speaking solely of the consumer finance field?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No, not necessarily. I just referred to the consumer field to show that there apparently had been some change of legal opinion. I would like to know if you consider anything else in setting your interest rates than what you consider to be a reasonable profit on your operations.

Mr. PATON: I would think that is a correct statement.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Did you only consider the profit?

Mr. PATON: We considered the total cost of the money to us plus a reasonable profit.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well, Mr. Paton, just now you told me you did not consider those in setting your interest rate; you considered this was something quite separate. This is the point I want to have clearly stated.

Mr. PATON: My contention was that we treat the cost of operating such loan accounts on one side; we treat the actual gathering cost of funds to provide these loans on the other and I would say it is quite likely that each bank would include in that cost of interest, a reasonable profit on the gathering of the funds. I did not say that we lent the funds at exactly the same figure they cost us, if you follow me.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I still am not clear, Mr. Paton, if you consider anything, in setting your interest rate, in addition to your reasonable profit of operation. I am unable to find out why you include some things and do not include others and still continue with your service charges and compensating balances. Could you give me the distinction?

Mr. PATON: I do not want to confuse the issue any more than it has been, and we have been around this area for quite some time.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I am sure we are both trying to clear it up, Mr. Paton.



Mr. PATON: We certainly are, Mr. Cameron. The interest cost to a borrowing account which has relatively no activity does not necessarily differ from the interest charged to an account which has activity. I am speaking of the operating account on which we charge service charge if applicable. In normal times we have a prime rate of say  $5\frac{3}{4}$  per cent or whatever the rate happens to be, and that is the interest rate which is awarded to all companies in that category.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But when you speak of an interest rate which is awarded—I think charge might be a better term; still I will take your term “awarded”—to certain categories, then this implies that you take into consideration some other factors in setting that interest rate than just profitability. What are the other factors, the cost of servicing the account?

Mr. PATON: Would you like Mr. Coleman to answer this question?

Mr. COLEMAN: Mr. Cameron, I would think the two main ingredients in deciding the interest rate on a loan are: (1) the cost of the money to the bank, and (2) the quality of the risk. It is true, when you are in a tight money period like we have been, that it has not been possible to pay much attention to the quality of the risk, and your man with undoubted security, your first class risk, pays the same as your poorest risk. But in a normal money period, the two main ingredients are the cost of money and the quality of the risk. Perhaps this is an over-simplification, but if you isolate your lending operations, what a bank has to do is to try and get a margin between what they pay for the money and what they charge for it which will pay their normal operating expenses and return them a reasonable profit.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): What are the normal operating expenses? Are they not these things that I set out here: salaries, rent, light, heat?

Mr. COLEMAN: I would say yes to that. I do not know if Mr. Paton feels the same.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): They must be considered.

Mr. COLEMAN: You have to allocate a certain part of your expenses to different departments of your operation.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes.

Mr. COLEMAN: And your loaning department would certainly be included there.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): In the final analysis, when you have done this allocating, then this enables you to set an interest rate?

Mr. COLEMAN: That is right, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Can you tell me why you exclude certain of these things from your interest rate and recoup yourself by other means, by means of the compensating balances and the service charges. If I recall correctly, Mr. Paton told us last week that the incidence of compensating balances has been increasing lately.

Mr. PATON: That is right.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Could you tell me why they are excluded.

Mr. COLEMAN: I think service charges relating to loans apply only to consumer loans, and this is a much more expensive type of operation than an ordinary wholesale type of loan.

The CHAIRMAN: Mr. Coleman, why does your paper not refer to service charges on current accounts?

Mr. COLEMAN: A current account is a deposit account, Mr. Chairman. I think we are talking about the loaning end of the business now. A current account is a deposit account.

I forget where I was. Did I complete my answer.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No. I hope you had not.

Mr. COLEMAN: Will you tell me what was left unsaid?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I would not dream of putting words in your mouth, Mr. Coleman.

The CHAIRMAN: I did not think my intervention was that sharp.

Mr. COLEMAN: Mr. Chairman, I am not sure where we left off.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I was asking you how you differentiated between these various costs in setting your interest rate, what criteria you used and why you excluded some elements of cost and included others? I also asked why, in recent years according to Mr. Paton last week, the incidence, for instance, of the demand for compensating balances has been increasing if it is not, as I suggested to Mr. Paton last week, a means by which you were able to place yourself in a better competitive position with the rising near banks?

Mr. COLEMAN: I think I was saying that the service charges, so far as I know, apply only to consumer loans and this is a more expensive type of operation—if you have a payment coming due every month and if you write one or two letters or make a couple of phone calls, you do not make any money, you lose money. That is all I know about service charges. I do not know of any other loaning accounts where there are service charges.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Is there anything at all which prevents you from taking an account of these costs—about which you must know a great deal—and including it in your interest rate so that your customer knows what he is going to pay in interest charges?

Mr. COLEMAN: No, I would say not and I even think it would be desirable that we show the true effective charge. I think this would be desirable and the banks, to my knowledge, never have refused this if a way could be found to do it and if all lenders would do the same thing.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I am glad to hear you say that, Mr. Coleman, because last week you said you did not anticipate any change in the policy of asking for compensating balances or imposing service charges if and when the ceiling on interest rates is removed. I am a little at a loss to understand why this should be so.

Mr. COLEMAN: Mr. Cameron, in talking about an effective cost I was not including compensating balances. I think it would be difficult, if not impossible,

that if the day came when we related compensating balances to loan accounts and we had to try to show the effective cost to the borrower, because then the cost of money enters into it, and this is a fluctuating thing from day to day. But from a service charge standpoint, I do not think there would be any problem.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I still would like to understand why it would not be possible with the compensating balances. What are your criteria for establishing the size of the compensating balances?

Mr. COLEMAN: This first comes from an analysis of the account. I have the form here. This form is called "An analysis of a current account". At the top it shows the work done in the period for this customer: deposits received and credited to the account at 10 cents each; items deposited which were cleared to other banks, and there is a 4 cent charge per item for that; currency deposited, and there is a charge of 95 cents per \$1,000; coin deposited takes more work so the charge is \$1.80; cheques issued and debited to the account carry a charge of 10 cents. Then total charge for work done in the period; revenue from the account in the period; service charges collected or due; exchange on out of town cheques collected; total revenue and then uncollected portion of charge for work done in the period. Then, calculation of average daily amount in float—these are the cheques which have been issued and which have been floating around the country and not actually charged up to the account. The total value of items deposited; the total value of transfer of customer's fund for the period. Then, we calculate the additional balances required, and this is what you are asking. We take account of the net average daily balance after allowing for the daily amount in float. The average daily balance required to be maintained to cover the uncollected portion of the charge for work done in the period is the compensating balance.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): This is the balance which is to be maintained from that point forward on the basis of past experience?

Mr. COLEMAN: Mr. Cameron, the custom is to analyse the account for a particular month. I do not think any bank does it every month because it is quite a job. You do it for the month and then if it seems there is more activity or there is to be maintained from that point forward on the basis of past experience?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): And the compensating balance may be varied?

Mr. COLEMAN: That is right, sir.

The CHAIRMAN: From month to month?

Mr. COLEMAN: I do not think it would, Mr. Chairman, because, say, you analyse the amount in March, and if the pattern of the account seems relatively the same, you might not analyse it for another year. There are two sides to this question.

The CHAIRMAN: I think it would be helpful, if I may say so, if this form could be circulated. You may not have it available at this moment but at least it would be easier to follow. I gather from that form that it is possible to have both a compensating balance and service charges.



Mr. COLEMAN: That is right. It could be one or the other or a combination of both.

The CHAIRMAN: Therefore, you can have service charges on other than personal loans, consumer loan accounts?

Mr. COLEMAN: Yes. This relates to the activity in the current accounts, Mr. Chairman. This is a deposit account, not a loan account, where cheques are issued, coin taken in, and so on.

The CHAIRMAN: So you do have service charges on other than consumer loans?

Mr. COLEMAN: Oh, yes.

Mr. FULTON: Do you have a compensating balance in a deposit account? I thought you only had a compensating balance in a loan account.

Mr. COLEMAN: Oh, no. Quite the contrary they are more prevalent in deposit accounts.

The CHAIRMAN: Mr. Coleman, if Mr. Cameron will permit me, I think this might be very useful to the Committee. May I refer you, sir, to the submissions of your association to the Royal Commission on Banking and Finance, clauses 503 to 505 on page 111. Perhaps Mr. Perry might hand you a copy. These are the proposals of your association to the Porter Commission as reported on page 111 and if I may read your association's submissions:

Clause 503. Requiring compensating balances from borrowers fits into a discussion of interest rates because such a requirement is generally viewed as a means of increasing the effective rate of interest on a loan.

This is what your association told the Porter Commission.

This, however, is not necessarily the case. If the compensating balances required were no larger than the working balances ordinarily carried by borrowers nothing would be gained by requiring such balances. Only when compensating balances are in excess of ordinary working balances, would the cost of bank credit to borrowers be raised. This can be achieved more simply through higher interest rates, which are to be preferred because they state precisely the cost to the borrower. To require compensating balances disguises the true cost of credit to the borrower.

Mr. COLEMAN: That is right, I agree completely.

The CHAIRMAN: You would?

Mr. COLEMAN: This is a submission; I agree completely with it.

The CHAIRMAN: With all due respect sir, is this entirely consistent with what you told Mr. Cameron?

Mr. COLEMAN: I think so. We were not talking about loaning accounts; we were talking about deposit accounts.

The CHAIRMAN: That is right. Now let me go on to clause 504.

It might be argued that compulsory compensating balances would have the advantage of requiring borrowers to maintain balances sufficient to compensate the banks for the activity in their accounts.

I ask the Committee to listen to this.

The best way to achieve this, however, is to levy service charges on all clients, including borrowers, who fail to keep adequate balances to cover the cost of managing their accounts. This permits an individual approach aimed directly at the accounts concerned and is a fairer approach to a uniform provision for compensating balances.

I read this to you and to the Committee, because you appear to have just told us that you foresee situations where there are either compensating balances or service charges or both. I think what concerns Mr. Cameron and perhaps other members of the Committee as well, is that with your desire to have a freeing of the interest rate, you also intend at one and the same time to have service charges and compensating balances for the same customers' general activity, whether it involves two accounts, three accounts or four accounts.

Mr. COLEMAN: All I can say, Mr. Chairman, is that. I do not think any bank wants to gouge the public. We certainly do not, and I think my colleagues share the same view. All we want in one form or another, is proper compensation for the work we do and the services we provide, and if we got a higher interest rate and in that way were compensated, probably there would be no stipulation for compensating balances on loan accounts, although this has been a habit in the United States, a practice for many, many years. It is a rare borrowing account in the United States where there is not a stipulation for compensating balances. As I said the other day, we have thousands of accounts on our books where we insist on compensating balances where there are no loans to the borrowers.

Mr. LAMBERT: Unfortunately Mr. Coleman said a compensating balance on a loan account. With the greatest respect, there is no such thing. A loan account is an entry on the asset side of the banks' books.

Mr. COLEMAN: But it could be related to a loan account, Mr. Lambert.

Mr. LAMBERT: Yes, but unfortunately a number of the Committee members are confused, when you do not distinguish between a loan account, which is an asset matter and a deposit account, which is a liability item. Certainly a deposit account may have deposits arising from a loan coming in to it. Certainly, I could write 100 cheques in my deposit account which had originated from a loan in part and cash from other sources, but someone who took an equal loan, might only write 5 cheques this month and, therefore, I should be charged more for the processing of my account than the other person.

The CHAIRMAN: I think that is a very useful comment. I just want to bring to the attention of the Committee the fact that this submission to the Porter Commission by the Banker's Association seems to say that on deposit accounts—and I presume this is what your association was referring to—banks should charge either compensating balances or service charges and that service charges were preferable. I have waited throughout the day before bringing this to the attention of the Committee, hoping that this question would be clarified, but it appears more and more obvious, with all due respect, sir, that it was the intention of the banks in Canada to be prepared to charge both, whatever the interest rate might be together with a service charge and a compensating

balance—not necessarily in every case, but it certainly would not be an uncommon practice. As I say, this appeared inconsistent with my reading of your submission to the Porter Commission. I felt it wise to bring it to the attention of the Committee.

Mr. COLEMAN: I am not sure, Mr. Chairman, just what is intended. Is this just a paragraph or paragraphs to develop what compensating balances are, or is it a recommendation? I have not seen the front of this and I have been trying to get the sense of it. It is out of context to me, so I cannot comment intelligently.

The CHAIRMAN: It is headed "Submission to the Royal Commission on Banking and Finance by the Canadian Bankers Association," and appended to it are submissions by certain bank presidents. The part I have read to you is part of your association's submission to the Porter Commission. I take them as they are printed.

Mr. COLEMAN: So that is what it is; I did not know whether it was from any one of these other names mentioned here.

The CHAIRMAN: No, it is from your association.

Mr. COLEMAN: It seems to me that this is clarification. They are not talking about practice; they are talking about clarification.

The CHAIRMAN: You seem to be making a recommendation to the Commission at that time as to the most appropriate banking practice. I could be mistaken, but I interpret this, and I ask the Committee to make their own interpretation, as saying that service charges are better than compensating balances to take care of the type of expenses which Mr. Lambert referred to, and that in effect you are not suggesting that both should be used. I do not think you are referring to existing practices; I am not suggesting that.

Mr. COLEMAN: I do not intend, or I did not intend to suggest that both would be a requirement. So far as we are concerned in our bank, we would give the customer the choice and we do give the customer the choice. We will ask him to either pay a service charge to compensate us for the operation of the account, or we will give him the choice of maintaining a balance to compensate us. We will have the use of the money to put to work and it should return us approximately the same amount as the service charge would return.

The CHAIRMAN: What about a standby charge to the line of credit. Would you charge that as well?

Mr. COLEMAN: Oh yes. That is a completely different thing. A standby charge is a common thing to ensure the customer that he has credit available when he wants it.

The CHAIRMAN: Would you mind turning to paragraph 101 at page 20:

On the other side, however, there are a number of reasons why the banks are reluctant to impose stand-by charges on all lines of credit. As long as the line does not have a contractual status, the bank knows that it can protect itself by reconsidering credit facilities if necessary. If a fee were exacted, the bank might, in the absence of protective provisions, be legally committed, even if circumstances changed drastically. Normally there are wide fluctuations in each loan account over the period of a year.



For example, a customer may buy inventory and require working capital to finance it, then when he sells the inventory, he may still need funds to finance his receivables. Finally, the loan is paid off. Such fluctuation in an account is a healthy sign. If the customer had to pay a stand-by charge, he might borrow the full amount and try to employ the funds somehow even when he did not need them in his operations. This would make it difficult for the bank to have a proper understanding of his position and, more important, would deprive the banks of one of the big factors in their flexibility.

This is your association's submission to the Porter Commission.

Mr. COLEMAN: That is entirely consistent with anything we have said. A standby charge is a charge at, let us say, one half of one per cent, to let the customer know that barring any dramatic change for the worst in his financial position, the line is available. Let us assume a company had a line of credit of \$1 million, they were not paying a standby charge, and we get into a tight money period like we are operating in now. The bank might have to go to that client and say: "I am sorry, we just cannot leave this line open." But if that client were paying a standby charge, then it would only be exacted on the portion that he is not using. The bank could not go to him, and during this period of monetary tightness, banks are reluctant to set up credit on a standby basis because of our possible inability to make the lines available when they are needed. In normal operating times, with good clients, we would not hesitate to set up standby credits. Today though, it is a little different.

The CHAIRMAN: Has it been the general practice in the past to have standby charges?

Mr. COLEMAN: I would think so, although very few clients relatively avail themselves of this facility, and it only applies—I think I am right in saying this—to large clients. You do not get small borrowers asking for standby charges; it is usually people who are borrowing substantial amounts.

Mr. FULTON: It is more important to them to have it in times of tight money than it would be in ordinary times.

Mr. COLEMAN: And this is why they like to have standby arrangements during tight money periods. We have had requests which we have had to decline because we could not be sure we would be able to take care of the requirements.

The CHAIRMAN: What if I told you that information has been conveyed to me that customers in Windsor who have had lines of credit over several years have been asked to pay standby charges on them?

Mr. COLEMAN: Mr. Chairman, that would be to ensure that the line would be available when they want it.

The CHAIRMAN: All right; thank you. Mr. Latulippe, you are next.

*(Translation)*

Mr. LATULIPPE: Mr. Chairman, I have some remarks to make and some questions to ask which are very basic and elementary...

The CHAIRMAN: Mr. Latulippe, you know we are on the general interest rate, you know that?

Mr. LATULIPPE: Yes, I am going to speak about interest rates. I would like to ask these gentlemen to tell us who owns the money, to whom all this money belongs to?

(English)

Mr. PATON: Perhaps Mr. MacIntosh could answer that, Mr. Latulippe.

Mr. MACINTOSH: May I ask for a repetition of the question, Mr. Chairman?

(Translation)

The CHAIRMAN: Would you repeat the question, Mr. Latulippe?

Mr. LATULIPPE: I would like to know who owns all the money, to whom does all this money belong?

The CHAIRMAN: Who is guilty?

(English)

Mr. MACINTOSH: The general public own the money supply in the economy, Mr. Latulippe.

(Translation)

Mr. LATULIPPE: Could you tell us in that case if all the money in circulation comes from the banks and if so, if it must not necessarily return to the bank? If it goes back to the bank, can you tell me whether or not it is increased by the interest?

(English)

Mr. MACINTOSH: I think there were two or three questions there. The first question was: Is all the money in the banks? I would say no; the money supply consists not only of the deposits in the banks but of the currency in circulation, the bank notes, and also I would include all the chequing deposits of near banking institutions, which are also money inasmuch as they are used as a medium of exchange for payment, have a store value and, in that sense, they are money.

(Translation)

Mr. LATULIPPE: But when this money is born, who has the authority to give it birth? Money is created somehow or other; it actually exists, so somebody had to create it. Is that person the owner of the money?

(English)

Mr. MACINTOSH: If I understand you correctly, you are going back to the subject of the origination of the supply of money, and this is a matter for the central bank. Once deposits come into existence, then the people who own those deposits control them, and they are then capable of transferring ownership of those deposits from one to another by means of the cheque system or by means of passing currency from hand to hand. A cheque is an order of payment which directs a bank to make a payment from A to B, and the ownership of the money is in the hands of the depositors or of note holders.

(Translation)

Mr. LATULIPPE: Could you tell us, since citizens have to repay capital which is borrowed, plus the interest which they did not borrow, what happens if they fail to meet their obligations?

(English)

Mr. MACINTOSH: Well, sir, we hope that they will be able to fulfill their obligations. When we lend them money, yes, we certainly intend that they should not only pay back the capital at maturity but return us an interest over the period of the loan. We presume that when they make the loan they have some productive activity to engage in which will return them a rate of interest sufficient to pay the loan, or if they are consumers, that their incomes will be adequate to make payment of the loan over time. We certainly hope that would be the case.

(Translation)

Mr. LATULIPPE: Since they are not producing the money nor the interest, where are they going to get this surplus, which is the interest, in order to reimburse both capital and interest?

(English)

Mr. MACINTOSH: Individual families and units do not have to be capable of manufacturing money or creating it, in order to earn it. We are all, as family units, in the position of having to earn income from productive effort, which provides us with an income; the income is, in some cases, used to repay loans from banks or others, but no individual or private corporation in the economy is a money creating unit. The money creating function is a function of the central bank.

(Translation)

Mr. LATULIPPE: Would it be possible to find out whether the borrower has to repay more than he got? In other words, does the borrower have to repay more than he received?

(English)

Mr. MACINTOSH: Yes, he has to repay his principal plus interest as well; therefore, he is repaying us a rate of return when we make a loan to him. I hope this is the case with other borrowers as well, at least I think it is their intention. In order to do this, presumably he has some form of activity which is going to earn him an income with which to make the interest payment. The individual borrower does not, in any sense, have the capacity to create the wherewithal to remake his payment, except by his activity or labour.

(Translation)

Mr. LATULIPPE: In this case, if citizens have to reimburse the money that they have borrowed, in addition to the interest, and if all citizens have to do this, how much then will they have to pay and where will they find the money to do this? In other words to repay more than we have borrowed? If everybody has to do this, how will they find the money to do it? It is very difficult for people to reimburse more than they have received.



(English)

Mr. MACINTOSH: The sum of interest payments in the economy by borrowers are equalled by the sum of interest receipts by lenders so there is no problem about raising the money. Income equals expenditure in the economy as a whole. This is true not only of interest but of all other forms of income.

(Translation)

Mr. LATULIPPE: Could you tell us whether it is because of this that there is mortgage piled on mortgage and a constant increase of private as well as public debt?

(English)

Mr. MACINTOSH: If I understand you rightly, you are asking why is there an increase in debt as the economy continues to grow. I think the reason is that the growth in debt represents the increase in real assets which come into existence when people borrow money and create things. The amount of mortgage debt in the economy, plus the amount of debts of provincial and municipal governments, plus the amount of debt of corporations, plus the amount of debt of individuals, is far greater than it was 10 years ago, and I hope it will be far greater than that in another 10 years, because this would imply that there are assets on the other side which have been created out of the debts.

(Translation)

Mr. LATULIPPE: Is it logical for a country to get into debt and for provinces, governments and individuals to get further and further in debt?

The CHAIRMAN: This is a question of general economic policy and I wonder if you could get a little bit closer to the general sphere of interest rates charged by banks to their clients?

Mr. LATULIPPE: We can therefore conclude, Mr. Chairman, that banks create money readily. There is no doubt about this at all because the debt of all Canadians, of all Governments, amounts to 87 billion whereas the legal tender issued by the Bank of Canada amounts to only 2 billion 500 million. This is undoubtedly creation of credit and this credit brings in interest. Here I am coming back to the subject.

(English)

Mr. MACINTOSH: Mr. Chairman, I thought that was a lengthy non sequitur.

(Translation)

The CHAIRMAN: At the same time, Mr. Latulippe, we have had a very interesting discussion on the creation of credit. After having finished that discussion on the statements of the bankers, I think it is the intention of the Committee at this point, to try and limit discussion more precisely to the question of interest rates on commercial and other loans.

Mr. GRÉGOIRE: Mr. Chairman, if I can help you to understand the meaning of the question I was listening to the English and French of both, and what Mr.

Latulippe means in fact is that on the whole—and not only for one individual—when there is a total amount lent that total comes from new credit created somehow or other. I do not want to pose that problem right now, but this appears to come from new credit which accumulates from year to year. Now interest charges are being levied on the new credit itself, which was not created. Now what Mr. Latulippe means precisely, is that when an individual personally—and here I am coming to the point—borrows to repay the capital and the interest it is because another individual besides him had to go into debt in order to bring in new credit into circulation to allow the first individual to repay capital and interest. This has been snowballing for several years and now today the debt is very high, for the Government in general, much more than for the money supply, if only to pay interest governments have to make further borrowings.

The CHAIRMAN: I suppose the banks hope that this snowball is going to remain frozen.

Mr. GRÉGOIRE: That is what made me speak as I did a little while ago, when Mr. MacIntosh was saying that debts are increasing because assets were increasing. I think Mr. MacIntosh is not quite right, because we still have debts.

The CHAIRMAN: Mr. Grégoire, excuse me, I allowed you to help the Committee to understand Mr. Latulippe's questions, and I thank you for this, but I think now I should ask Mr. MacIntosh and also Mr. Rodgers whether they can answer this question.

*(English)*

Mr. FULTON: Is it not a fact that what is being discussed here is the creation of credit and the amount of credit at the total disposal of the country? Is this not really where the Bank of Canada comes in and, by controlling monetary policy and the reserves kept on deposit, they do control the power of the banks to give credit? Is this not a question, really, which comes back more to the Bank of Canada and fiscal monetary policy?

The CHAIRMAN: I think you have raised a very good point, Mr. Fulton. Perhaps if Mr. MacIntosh can give a brief answer to Mr. Latulippe's question we then will invite Mr. Latulippe to continue. This may be the best way of getting out of this particular impossible procedural impasse.

Mr. MACINTOSH: I am not sure I know what the question was.

The CHAIRMAN: I think that Mr. Latulippe, assisted by Mr. Grégoire, posed the problem that when someone repays principal and interest he, in effect, is taking it from someone else, and so on, and this creates some type of snowball.

Mr. MACINTOSH: Thank you for the clarification.

The CHAIRMAN: You are welcome.

Mr. MACINTOSH: I think this snowball is running away.

The CHAIRMAN: You could make a brief comment now and we can return to this when we have some Bank of Canada people back with us.

Mr. MACINTOSH: Mr. Chairman, I will only say briefly, then, that the process of expansion of credit in the economy which makes possible the payment of

interest is no different from the process of expansion which makes possible the payment of larger salaries and wages, or any other form of income.

(Translation)

The CHAIRMAN: You may ask your next question now, Mr. Latulippe.

Mr. LATULIPPE: Mr. Chairman, I am referring directly to the rate of interest as defined on page 47, clause 71: "eight per cent per annum on the paid up capital" In the first sub-clause, paras (a) and (b) reference is made to the paid-up capital. Eight percent may be paid on that, but no more unless the bank has a net account equal to 30 percent of the paid-up capital. So, Mr. Chairman, if paid-up capital and paid-up capital stock mean the same thing, why use both words?

If the Bank has a paid-up capital of ten million dollars, then it must have a general reserve of 3 million, to pay 3 percent dividends. When a bank pays \$3.00 on a \$10.00 share, or 40 percent someone is getting something out of this and the banks will make even more profit at a loan at more than 6 percent, without any ceiling. They have made profits that enable them to pay dividends of 30 percent, besides having a net account of 30 percent. If they have made such a profit with the present ceiling at this time is there any justification in allowing them to make even more dividends, up to 50 or 60 percent, and to increase the value of their shares and equity?

Mr. LAVOIE: Mr. Latulippe, you refer to Section 71. It is clearly mentioned that no dividend or bonus must be declared should the capital be impaired. A while ago, you were speaking of a capital of ten million dollars. If, by paying a dividend, you were to impair the capital, this would be prohibited by the Act. That cannot be done. The directors would incur a personal liability in this regard. It says here "the directors who knowingly and wilfully concur in the declaration of any dividend" contrary to sub-section 1 are jointly and severally liable". This is clearly stated in Clause 71, sub-clauses 1 and 2. It is not a question of a rate of interest, it is a question of dividends on paid-up capital. The question of the rate of interest paid to the client is another matter.

Mr. LATULIPPE: We can understand from that, Mr. Chairman, that apart from having a net account of 30 percent the banks have made this profit with a ceiling of 6 per cent. Why do you want to make a change today if there is a reasonable profit from this?

(English)

The CHAIRMAN: Who would like to deal with that one?

(Translation)

Mr. LAVOIE: With regard to the removal of the ceiling, if you refer to the brief submitted by the Bankers' Association, you will find on page 3, for instance, the main reason for this recommendation. They say that "the 6 percent ceiling impedes the flow of credit to some borrowers and—by driving them to higher cost lenders—frequently harms the very people it is designed to help."

Mr. LATULIPPE: What difference would there be if you asked the same rates?

Mr. LAVOIE: What rates?



Mr. LATULIPPE: If you are asking for the same rates as the finance companies or—

Mr. LAVOIE: I do not think it is a question of such rates as the finance companies have been applying, but it is simply applying the rate of interest that we apply to loans according to the present cost of money.

Mr. LATULIPPE: Yes, in October 1939, for instance, the Federal Government asked 80 million dollars of the banks for war purposes. They gave the government that amount without depriving anybody of anything. If this could be done then, could it be done, at the present time when everyone has difficulty in finding capital, when the rates of interest are much higher than they were?

The CHAIRMAN: Would you repeat the question, please?

Mr. LATULIPPE: In October 1939, when the war broke out the government needed money, they could not get enough of it. There were great difficulties in those days, if I remember well. The minute war was declared, the government asked the banks for 80 million, and the banks advanced 80 million dollars without taking anything away. Where did they get the money, for that new issue?

The CHAIRMAN: Mr. Latulippe, I think that this question is quite interesting, it is a matter of history, but at the same time, allow me to suggest that it has to do with the policy of the Bank of Canada rather than with the interest rates. Let me ask you, please, to pass on to another question.

Mr. LATULIPPE: This takes into account the rate of interest, because in 1941, the government had to refund the 80 millions plus three millions in interest in addition to the capital.

The CHAIRMAN: Yes, but we have received a few suggestions from the government with the idea of allowing a higher rate of interest in some cases. The bankers having given us some statements, and expressed some points of view in this connection we have asked the members of this Committee to put questions in connection with this bill C-222. Your question is an interesting one, as I said, but it deals with general economic policy. I am almost sure that there will be a representative of the Bank of Canada who will appear before this Committee before we have finished our discussions. You could keep that question until that representative appears here.

Mr. LATULIPPE: I shall certainly revert to that later. There are a lot of things that we could deal with, but I do not want to take too much time. Before finishing, if the system is such that the refund must exceed the amount borrowed, if there are more births than deaths and more destruction than creation, what happens? If the banks have the power to issue money, then they can also, put it away. What has interest to do with all that?

The CHAIRMAN: What interest has to do with all that?

Mr. LAVOIE: It would be a little difficult to put money in a coffin. I doubt anybody would do that.

The CHAIRMAN: I think the witnesses did their best to answer these questions, but for the time being I think that I will ask Mr. Laflamme to speak.

(English)

Mr. LAFLAMME: I have only a few questions, Mr. Paton. I would like some clarification on the figures you have already produced in the "Table of Costs for a Personal Instalment Loan or Advance in the Principal Amount of \$1,000".

Mr. COLEMAN: Do you mind, Mr. Dixon, coming up here? He is the expert on this.

The CHAIRMAN: By the way, for the record, I think there was some reference to the witness who is going to sit down being "Mr. Nicks". Now, perhaps the witness may wish he were in Mr. Nicks' position because Mr. Nicks is president of the Bank of Nova Scotia, and who knows what the future may hold. This is without prejudice to your colleagues who are here. I think the name was Mr. Dixon, if I am not mistaken. What is your position, sir?

Mr. W. J. DIXON (*Deputy General Manager, Bank of Nova Scotia*): I am Deputy General Manager of the Bank of Nova Scotia.

Mr. LAFLAMME: I would like to have some clarification of the calculation you have made of those figures. You say on a loan of \$1,000 the total loan cost is \$52.48. Is that the cost to the bank?

Mr. DIXON: That is the cost to the borrower.

Mr. LAFLAMME: To the borrower?

Mr. DIXON: Yes, to the borrower.

Mr. LAFLAMME: What would be the total interest cost on the total payment after one year on a loan of \$1,000?

Mr. DIXON: As it says below, the total loan cost to the borrower is \$52.48. Dealing with Bank "A" the interest portion of that cost is \$33.13.

Mr. LAFLAMME: What is the rate?

Mr. DIXON: It is six per cent simple interest on the reducing principal balance.

Mr. LAFLAMME: Plus?

Mr. DIXON: That is the interest cost, six per cent simple on the reducing principal balance. Starting with \$1,000, and reducing it to nothing, the interest cost is \$33.13.

Mr. LAFLAMME: In one year?

Mr. DIXON: Yes, in one year.

Mr. LAFLAMME: I just cannot understand the calculation.

Mr. LAVOIE: The service charge is \$19.35?

Mr. LAFLAMME: The sum of \$52.48 is the total of \$33.13 plus \$19.35.

Mr. DIXON: That is right, but the interest portion, as I am trying to point out, is \$33.13; the service charge portion is \$19.35.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would it be correct to say that that charge is on an average balance of \$500 for a 12-month loan?

Mr. DIXON: Which charge?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The \$52.48. On the diminishing principal that is owed, the average would be \$500 throughout the year?

Mr. DIXON: Yes, roughly.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): So the effective rate of interest would be about 10.4 per cent?

Mr. DIXON: That is right. The total charge is \$52.48 and, as you say, on the average the borrower has had the use of approximately \$500, relating the \$52 to the \$500, it comes out to approximately 10 per cent.

Mr. LAFLAMME: Suppose I borrow \$1,000 and I reimburse in 12 instalment payments, what will be the total amount I will reimburse to you after one year.

Mr. DIXON: \$1,052.48.

Mr. LAFLAMME: I see.

Mr. DIXON: In 12 payments.

Mr. LAFLAMME: Mr. Chairman, may I ask a question of Mr. Elderkin?

The CHAIRMAN: Yes.

Mr. LAFLAMME: Does your office have any information or legal opinion regarding the service or the administration charges of the banks?

Mr. ELDERKIN: Yes, Mr. Laflamme. There was a legal opinion given by the Department of Justice that if there was an expressed agreement between the bank and the customer, the service charge was legal. I recall an answer in the house too, by a former minister of justice, to this effect.

Mr. LAFLAMME: If there is an agreement.

Mr. ELDERKIN: If there is an expressed agreement between the bank and the borrower. This follows the term of the wording of section 93(3), where it requires an expressed agreement between the bank and the borrower before any service charge.

Mr. LAFLAMME: Then this is the reason that when someone borrows something he has to sign a contract with the bank.

Mr. ELDERKIN: That is correct.

Mr. LAFLAMME: This legalizes it.

Mr. ELDERKIN: That is correct.

Mr. LAFLAMME: But, Mr. Paton, if you have the right within the law to put on your own service or administration charges, then do you need the removal of the ceiling? Why not increase your service charges to compete with the other institutions?

An hon. MEMBER: That is a nice question too.

The CHAIRMAN: I think somebody should answer that!

Mr. PATON: The entire question of requiring the removal of the ceiling, Mr. Laflamme, is not devoted entirely to the lending side of our operations. We have a world wide situation, where interest rates are higher. We are excluded from participating as we should to the full extent of our operations as a result of this unnatural 6 per cent ceiling. The problem regarding service charge or how we recoup from our borrowers is not by any means the entire story; in fact it is not the major part of the story. The entire problem is the removal of this



artificial limit so that we can participate fully in the business we should be doing. In this type of freer operation we will have a flexible interest rate to cover the administration costs of this kind of borrowing.

Mr. LAFLAMME: Well, I have no other questions except that I do not understand clearly the legality of service charges. I understand that many other financial institutions, which do not have to respect the Bank Act, have increased their service charges in various fields. The banks are doing the same. If it is legal, why is it so important to have the removal of the 6 per cent interest rate.

The CHAIRMAN: Do any of you gentlemen wish to make any further comments?

Mr. PATON: It would be quite a natural rate of interest to be dealing with, Mr. Laflamme, on the basis that you suggest. Service charge, as we have endeavoured to point out, is the charge for services performed by the administration for the cost of this service. It would not be applicable throughout general lending in all industry and all countries. This is merely one section of our lending and relatively important too, but it is not the major section of lending.

*(Translation)*

The CHAIRMAN: I think that it is rather difficult to answer the question put by Mr. Clermont. You are going to ask your colleague's opinion Mr. Lavoie?

Mr. LAVOIE: Mr. Chairman, we have not had an opportunity to meet yet. I think that it will go to the end of the week and then, we will be able to get the necessary documents in order to answer the question that was put by Mr. Clermont.

*(English)*

The CHAIRMAN: Perhaps I might ask you to raise another point with them. I gather that it is the position of the Bankers' Association today that all the banks compete with one another very actively. Would you disagree with that statement?

Mr. PATON: No, sir; in fact we support it.

The CHAIRMAN: In that case, would it not be a tangible demonstration of this competition if you disclosed the names of the banks rather than just identifying them with letters? The press are covering our meetings and they are printed, and this may be a way of encouraging the public to see whether you are most competitive.

Mr. LAVOIE: So far as my bank is concerned I have no objection.

An hon. MEMBER: What about the other banks?

The CHAIRMAN: Is there any reason why you would not favour using the names of the banks?

Mr. PATON: These statistics can be gathered from any individual bank. I think the majority or all of them would agree. I, personally, would have no objection, but I could not speak on behalf of my colleagues.

The CHAIRMAN: Well, I would say that you are going to have a meeting to discuss how to answer the point raised by Mr. Clermont. I just made a suggestion because I was thinking about this. As I say, it seems to me that it would be

a wonderful opportunity for you fellows to compete for some business through the coverage of the meetings of this committee by the various media. We may not have the time to visit each of you. As I told members of the Committee, any one of them could visit a branch of each of your banks and get this information.

Mr. PATON: May we take your request under advisement and come back to you with it. I think this is a reasonable request you have made.

(Translation)

The CHAIRMAN: Mr. Laflamme has finished, I now recognize Mr. Grégoire.

Mr. GRÉGOIRE: Mr. Chairman, in one of the arguments advanced by the chartered banks to increase their rate of interest, there is that of competition from the near-banks. If a trust company lends at 9 per cent, and it needs deposits, it will be easier for it to give 6 per cent to its depositors. As the chartered banks are limited to a 6 per cent interest, it is evident that they cannot lend at 6 per cent interest as the near-banks can. I think that it is one of the main arguments made by the chartered banks for the removal of the ceiling on the rate of interest. Is that not one of the main arguments?

Mr. LAVOIE: Yes, it is, Mr. Grégoire.

Mr. GRÉGOIRE: Is it one of the most tangible one?

Mr. LAVOIE: You see, for example, a bank wants to get deposits on which it pays a rate of interest of 6 per cent, it is obliged to maintain a primary reserve of 8 percent with the Bank of Canada and a secondary reserve of 7 percent in bonds which will bring in a little more than 5 per cent. The most should be over 6½ percent, and, therefore, if the ceiling remains at 6 percent the bank cannot compete with other financial institutions which may lend money at 6 per cent.

Mr. GRÉGOIRE: From what I understood the banks pay an interest to their depositors of approximately 3 percent?

Mr. LAVOIE: That is right, Mr. Grégoire.

Mr. GRÉGOIRE: On all deposits?

Mr. LAVOIE: No, not on all of them, Mr. Grégoire, only on savings deposits.

Mr. GRÉGOIRE: Only on the savings deposits.

Mr. LAVOIE: Yes, on the savings deposits only.

Mr. GRÉGOIRE: Which, according to the Bank of Canada review of October 1966, page 662, constitutes a deposit of \$10 billion, 228 million, and on such an amount you pay 3 per cent interest?

Mr. LAVOIE: There are two classes of deposits. There are the regular savings deposits on which we pay 3 per cent and we also have deposit certificates on which we pay a higher rate of interest.

Mr. GRÉGOIRE: There are deposits from the Government of Canada, for instance, which amounted to \$492 million in September 1966. Do you pay interest on these?

Mr. LAVOIE: On the deposits of the Government of Canada, there is no interest on the first 100 million dollars. For anything in excess of that the interest rate is based on the Treasury bonds yields less 10 percent.

Mr. GRÉGOIRE: There are also provincial governments deposits which amount to 426 million dollars. Do you pay interest on these deposits?

Mr. LAVOIE: Yes, on a certain category.

Mr. GRÉGOIRE: But not on all of them?

Mr. LAVOIE: No, I do not think so.

Mr. GRÉGOIRE: On personal savings, you pay interest?

Mr. LAVOIE: We pay 3 percent.

Mr. GRÉGOIRE: Now, other deposits are mentioned here. You pay interest on those certificates?

Mr. LAVOIE: These are commercial deposits.

Mr. GRÉGOIRE: Do you pay an interest of 3 per cent on those?

Mr. LAVOIE: On commercial deposits, Mr. Grégoire, we pay no interest.

Mr. GRÉGOIRE: So you have 5 billion 397 million dollars here on which you do not pay interest at 3 per cent, but when you lend that money at 6 per cent, then you have a margin of about 6 per cent, while the trust company will pay 6 per cent to all its depositors and lends at 9 per cent. This means a margin of profit of 3 per cent, is that correct for that part of the 5 billion 397 millions dollars to which you refer as commercial deposits?

Mr. LAVOIE: We do not pay any interest on those commercial deposits.

Mr. GRÉGOIRE: Then you have a margin of profit of 6 per cent, a gross profit since you re-lend at the same rate.

Mr. LAVOIE: I have figures here concerning the rate of interest paid by the chartered banks on savings deposits and the prime rate on loans and the margin between the two, between the prime rate for the rate of interest that we can make on loans and the rate of interest that we pay on deposits. This varies between  $2\frac{3}{4}$  and 3 per cent.

Mr. GRÉGOIRE: Between  $2\frac{3}{4}$  and 3 per cent, not including the service charges?

Mr. LAVOIE: No, they are not included.

Mr. GRÉGOIRE: And for the near-banks, do you have the same figures?

Mr. LAVOIE: I do not have any figures for the near-banks.

Mr. GRÉGOIRE: But if they give 6 per cent and lend at 9 per cent, they make 3 per cent, including the service charges. As far as you are concerned, you give between  $2\frac{1}{4}$  and 3 per cent, the service charges not included.

Mr. LAVOIE: Not including the service charges, that's right.

Mr. GRÉGOIRE: And they, it is 3 per cent including the service charges.

Mr. LAVOIE: It depends on the rate of interest that they charge and that they pay.

Mr. GRÉGOIRE: Now, Mr. Lavoie, could you tell us during 1965, for instance, the last full year, how much the chartered banks as a whole, the eight chartered banks, how much have they paid in interest to their depositors, in absolute figures?



(English)

The CHAIRMAN: I believe Mr. Elderkin has it. Would you care to provide it for us?

Mr. ELDERKIN: In the fiscal year 1965 the bank paid interest on deposits of \$524.7 million.

Mr. GRÉGOIRE: May I have the answer again?

Mr. ELDERKIN: \$524.7 million.

The CHAIRMAN: \$524.7 million.

(Translation)

Mr. GRÉGOIRE: On the total average deposits in 1965?

(English)

Mr. ELDERKIN: I do not have the average deposits in 1965. The total deposits at the end of 1965 would not be particularly informative. It was about \$23 billion at the end of 1965.

(Translation)

Mr. GRÉGOIRE: You say \$23 billion?

Mr. LAVOIE: That is right.

Mr. GRÉGOIRE: Referring to the Statistical Summary of the Bank of Canada Canadian dollar deposits totalled \$18,594,000,000 for 1965, and further . . . Do you include in that the holdings of the bank and shares of shareholders?

Mr. LAVOIE: No.

Mr. GRÉGOIRE: What we have at issue here is \$20,792,000,000, including the holdings of the bank, i.e. the shareholders equity.

(English)

Mr. ELDERKIN: You mentioned that the Bank of Canada figures were in Canadian currency, and I am quoting all of the deposits of the banks.

The CHAIRMAN: Including foreign currency deposits?

Mr. ELDERKIN: Yes. I think that makes the difference.

(Translation)

Mr. GRÉGOIRE: On that total amount of 23 billion dollars in deposits, foreign and Canadian, you do not pay interest but when you calculate the interest at  $2\frac{1}{2}$  per cent approximately, on 524 million dollars you must subtract those deposits on which you do not pay interest—the commercial deposits as you say—which is 5 billion, 394 million dollars.

Mr. LAVOIE: No, we do not pay any interest on commercial deposits.

Mr. GRÉGOIRE: Are there other amounts on which you do not pay any interest? Could we know the total amount on which you did at the end of the year 1965? How much you had and how much you paid? This will amount to more than  $2\frac{1}{2}$  per cent but will increase to  $3\frac{1}{4}$  or even  $3\frac{1}{2}$  per cent. You are not paying interest on the 23 billion dollars but, 16 or 17 billion.

Mr. LAVOIE: I see your point of view, Mr. Grégoire, but I do not have the figure here. I cannot provide you with them immediately.

Mr. GRÉGOIRE: I did not say immediately.

Mr. LAVOIE: We would have to do the necessary research.

The CHAIRMAN: Perhaps you could give a reply later on.

Mr. LAVOIE: Yes, certainly, we will look into the matter.

Mr. GRÉGOIRE: Now, Mr. Chairman, with regard to the competition between the loan companies and the banks, will it not be possible to have a comparative table in this regard? Chartered banks have a margin of approximately 3 per cent between the rate of interest they pay and the rate of interest that they receive, plus the service charges. Could we not have the same information for the near-banks in respect of the interest that they pay and the interest they receive, and including the service charges. The committee might perhaps not contact the banks to provide us with that, since they do not know what is happening in the loan companies, but could the committee not get those figures since one of the main arguments put forward by the banks is based on the unfair competition they face from the loan companies.

The CHAIRMAN: Can you provide this information?

Mr. LAVOIE: If Mr. Grégoire will look at the report of the Porter Commission at page 59 (French version), he will see that the percentage of the bank revenues from loans, commissions, exchange, etc. is given for the years up to 1962. After 1962, we do not have any statistics. We would have to get them. We also have interest paid on deposits. You have all those figures at page 159 of the Porter report.

Mr. GRÉGOIRE: Are the service charges mentioned both for banks and loan companies?

The CHAIRMAN: Mr. Grégoire, you might be able to look through the report during the supper hour and then if you do not find what you want, we might consider your request. I think it would be preferable—

Mr. GRÉGOIRE: If you say that it is up to 1962—

Mr. LAVOIE: Up to 1962. Well, I do not remember—

The CHAIRMAN: I only have the English text here. Perhaps during the supper hour—

Mr. GRÉGOIRE: I have the French version here. Have I any time left?

The CHAIRMAN: About five minutes.

Mr. GRÉGOIRE: I will look at that and then I will be able to continue during the second round of questions to inquire the methods indicated here in support of the removal of the ceiling on bank interest. I think it is section 91, page 80 and following. Have you calculated, for instance, with the reports for 1966, what under Section 3, sub-section (b) constitutes  $1\frac{3}{4}$  per cent yield on per cent plus the short-term Government bonds? In the same report the Bank of Canada tried to determine the yield on short-term bonds. I found it quite difficult to establish that in spite of the tables we have. Could you say what this would represent at the present time? For instance,  $1\frac{3}{4}$  per cent plus.

Mr. LAVOIE: It is about 7 per cent, Mr. Grégoire.

Mr. GRÉGOIRE: At the present time?

The CHAIRMAN: I think, Mr. Grégoire, that Mr. Elderkin gave us this information.

Mr. LAVOIE: I do not think that what is mentioned here in paragraph 3 of clause 9, would be applied immediately. It would be based on the three months' average I would think.

(English)

Mr. ELDERKIN: On the rate plan, if this section is enacted, the rate will take effect only from the 1st of January, or in that half year ending June 30. It will be based on the average of a three month average, on the yield on the short term securities of Canada, over three months, ending November 30. Now, up to October 31, if the average rate is continued through November, this should probably, when adjusted to the nearest quarter, be five and a half per cent which, if you add one and three quarters to that, it would result in the rate of seven and a quarter for the first six months of 1967.

(Translation)

Mr. GRÉGOIRE: If I put that question, Mr. Chairman, it is because, at the present time,  $1\frac{3}{4}\%$  plus this average yield is approximately 7 percent; in other words, the present average is approximately  $5\frac{1}{4}\%$  per cent. But here is what is stated in Clause 91, sub-clause 9: "Where the average of the market-yield on short-term bonds of Canada for all Wednesdays in any period of three months ending on or after the 31st day of September, 1966, is less than four and one half per cent, sub-sections (2) to (8) and Section 92 expire on the 15th day of the month of such period but without affecting any loan or advance in respect of which a rate of discount has been charged before that day." This means that when the yield on short-term bonds is lowered to  $4\frac{1}{2}\%$  you would no longer be limited to a maximum of  $1\frac{1}{4}\%$  per cent over the average yield of such bonds for the three last months preceding that period. Is that what is meant by sub-clause 9?

Mr. LAVOIE: This means, Mr. Grégoire, that there will no longer be any ceiling on interest rates.

Mr. GRÉGOIRE: Since this  $1\frac{3}{4}\%$  per cent added to the average yield will no longer apply, this means that there will no longer be any ceiling.

Mr. LAVOIE: Exactly.

Mr. GRÉGOIRE: It would then be in the banks' interest to bring down the average yield of short-term bonds to  $4\frac{1}{2}\%$ ?

Mr. LAVOIE: It is a very difficult matter for the banks to establish the yield. This is done through the market, condition, etc.

Mr. GRÉGOIRE: That means that the submissions for the Treasury Bonds issued...

Mr. LAVOIE: No. Treasury bonds have nothing to do with it.

Mr. GRÉGOIRE: Yes, but it could help to reduce the yield of the securities. In that case, there would be fewer people to take up short-term bonds.



Mr. LAVOIE: They are two completely different sectors.

The CHAIRMAN: The Clerk has just told me that your time has expired.

Mr. GRÉGOIRE: I just have a minute or two more, Mr. Chairman.

The CHAIRMAN: Has Mr. Grégoire your permission to continue?

Mr. LAMBERT: Mr. Chairman, you should remind Mr. Grégoire that he is not a member of the Committee and can only speak after the members have spoken. This is a clearly established rule in all Committees.

Mr. GRÉGOIRE: Tell me the rule.

Mr. LAMBERT: That was adopted for almost all Committees.

Mr. GRÉGOIRE: If you have the written text. . .

Mr. LAMBERT: I have no text. This is a resolution. This is the policy that has been recommended in all committees ever since we have had this system of committees.

Mr. GRÉGOIRE: Mr. Chairman, I would ask Mr. Lambert to show me the resolution. It must be written down somewhere. Just let him show it to me.

The CHAIRMAN: Mr. Grégoire, I have been told that in some Committees, resolutions are carried to that effect. So far, as I told you a day or so ago, I did not think it was necessary to ask for such a resolution, but I would remind honourable members that there are certain responsibilities involved regarding their motions and amendments. I tried to make this distinction between members, and so far the members of the Committee did not feel it was necessary to have a formal resolution. But though it is true, as Mr. Lambert said, that there is a procedure which gives priority to the official members, we have so far been able to work without a formal resolution in this regard. If the Committee thinks that the time has come for a resolution, then I am in the hands of the Committee.

Mr. GRÉGOIRE: Mr. Chairman, I would like Mr. Lambert to tell me in what committees this resolution was adopted?

Mr. LAMBERT: External Affairs, National Defence, Trade & Commerce.

The CHAIRMAN: Mr. Grégoire, you might be able to continue this discussion later on. There might be some interesting opinions on this.

Mr. GRÉGOIRE: It is an important question, because I do not think there was any distinction made. There are no first or second class members. There is a distinction, and the distinction is made by the rules, and that is that those who are not permanent members of the Committee, cannot put forward amendments or second them in Committees. It has never been mentioned before, because the House did not want to make any distinction between first and second class members.

The CHAIRMAN: I would like, once again, to remind you that the House allowed the committee to make a distinction, if necessary, by resolution, between the official members and the other members who are present at the meetings, and take part in our work. As I pointed out a few days ago, you may agree that it would be easier to put this question in the hands of the Chairman, instead of having a formal resolution. It is entirely within the rules.

Mr. GRÉGOIRE: I would like the resolution to be moved to see if there really is a case. If this is voted, that distinction will have been made.

The CHAIRMAN: It is not a distinction between first and second class members, it is just a system or method of procedure which is just a little more restrictive than in the House itself.

Mr. GRÉGOIRE: May I continue with my questions, Mr. Chairman?

The CHAIRMAN: As I have just indicated to you, your time is up. You have had more than twenty minutes.

Mr. GRÉGOIRE: That is all right.

Mr. CLERMONT: You have asked if the Committee had no objection to giving him two or three minutes more. I said I had none. If we had given him that he would be through by now.

Mr. GRÉGOIRE: It was you who brought it up; I had nothing to do with it.

Mr. LAMBERT: Was there not an indication that we would now start on another round of questions, each in turn? I am quite willing to let him finish, as long as he stays with the subject.

Mr. GRÉGOIRE: I am entirely within the subject. We are dealing with Clauses 91 and 92.

The CHAIRMAN: If the Committee wishes to let you continue until six, I will offer no objection; I am in your hands.

Mr. GRÉGOIRE: So when the average yield on short-term loans will be lowered to  $4\frac{1}{2}$  per cent this will bring about a complete removal of the ceiling.

Mr. LAVOIE: At that point the ceiling will no longer be necessary.

Mr. GRÉGOIRE: We may therefore conclude that there will be every inducement to the banks to lower the average yield of short-term loans as quickly as possible?

Mr. LAVOIE: As I said a moment ago, Mr. Grégoire, the chartered banks have nothing to do with the fixing of the average yield of Dominion of Canada bonds.

Mr. GRÉGOIRE: Who does that?

Mr. LAVOIE: Market forces.

Mr. GRÉGOIRE: This means that chartered banks buy and sell on the money market. They may buy and sell money. Are they then in a position to influence that market to bring about a reduction in the  $4\frac{1}{2}$  per cent yield?

Mr. LAVOIE: I do not think so.

Mr. GRÉGOIRE: You do not think so?

Mr. LAVOIE: No.

Mr. GRÉGOIRE: So you tell the Government of Canada: "You are going to float a bond issue at two or three years. We are ready to buy at  $4\frac{1}{2}$  per cent". The Government will refuse, saying that they are being offered 5 per cent by other people—

Mr. LAVOIE: But that is not the way the Government goes about this. When it issues bonds we learn about it just as other people do, on that very morning.

We learn all about the amount of the loan, the conditions of the loan, the interest rate, etc. We do not dictate the conditions; we have never done so.

Mr. GRÉGOIRE: I have not claimed that you did, but you are in a position to influence the money market.

Mr. LAVOIE: Pardon?

Mr. GRÉGOIRE: I do not say that you lay down the conditions, but that you might be in a position to influence the market in order to bring down the short-term loan yield to  $4\frac{1}{2}$  per cent. Do you?

Mr. LAVOIE: I do not think so, Mr. Grégoire. Mr. Mercure tells me that the supply is  $3\frac{1}{2}$  billion in short-term Government of Canada bonds.

Mr. GRÉGOIRE: What does "short-term" mean exactly? Three years?

Mr. LAVOIE: Three years or less.

Mr. GRÉGOIRE: This means that in three years this supply of three billion dollars may be renewed and that during this process the banks, directly or indirectly may exert their influence to reduce the yield.

Mr. LAVOIE: I think I have answered that question, Mr. Grégoire; it is practically impossible.

Mr. GRÉGOIRE: If the Government should know that there is a group interested, at the present time, in taking up short-term bonds at  $4\frac{3}{4}$  per cent—at the present time it would be  $5\frac{1}{2}$  per cent. Would the Government not attempt to sell at the lowest possible rate?

Mr. LAVOIE: That is what the Government does all the time.

Mr. GRÉGOIRE: But if you say to the Government that you are ready to buy at  $4\frac{1}{2}$  per cent, without forcing them to sell at that rate?

Mr. LAVOIE: What you are saying is this. You are saying that if the Government were to decide to put an issue on the market at  $5\frac{1}{4}$  per cent for three years and that we, the banks, were to make a  $4\frac{1}{4}$  per cent offer—that would hardly be logical.

Mr. GRÉGOIRE: But would it not become logical if this lowering to  $4\frac{1}{2}$  per cent over a three months' period were to bring about the removal of the interest ceiling? Would it not be to your advantage to reduce the average yield over a three months' period?

Mr. LAVOIE: But as I told you a while ago it is not possible for the chartered banks to do that.

Mr. GRÉGOIRE: But as I said a while ago the Government always tries to make its bond issues, short, medium or long term, as the lowest possible rate of interest. Without forcing them in any way, you could tell the government that you are ready to buy at  $4\frac{1}{2}$  per cent?

Mr. LAVOIE: You could obtain a far more satisfactory answer from the officers of the Bank of Canada. They would probably be able to give you much more information.

Mr. GRÉGOIRE: Well, in that case, I will put my question differently. Would there be any advantage to the chartered banks in bringing the average yield down to  $4\frac{1}{2}$  per cent? Is that a fact?



Mr. LAVOIE: Mr. MacIntosh can answer that if you do not mind.

(English)

Mr. GRÉGOIRE: Could you answer this question, Mr. MacIntosh? Taking into consideration clause 9 of article 91—

Mr. MACINTOSH: I understood what you were saying.

Mr. GRÉGOIRE: —is it a fact that the chartered banks would profit if the average—

Mr. MACINTOSH: I understood your question.

Mr. GRÉGOIRE: —return went down to  $4\frac{1}{2}$  per cent? Would it be of interest to the chartered banks if such a situation developed for three months?

Mr. MACINTOSH: Mr. Grégoire, I would say that that would be a very expensive exercise and impossible to do. What you are saying is that in effect if the banks bought the whole of the short term debt of Canada, and you would have to buy all of it because nobody would fail to sell to you if you were buying, at  $4\frac{1}{2}$  per cent when interest rates are  $5\frac{1}{4}$  per cent. I can tell you with a great deal of certainty that we would buy every bond in the country at that rate. Therefore, we would have to buy the whole of this short term debt. But this would set up interest rate effects on all other classes of security which were of the same maturity and the same sort of relative quality, so we would buy not only the whole of the short term debt but the whole of the short term debt of the provinces, municipalities, corporations and everyone else, and we would also buy the whole of the international debt if anyone chose to sell it to us, because you cannot have two different markets. You have one level of interest rates for one type of an obligation and, therefore, we could have the whole of the United States debt dumped on us at that rate. I do not think our resources command that degree of ability to absorb the debt. In fact, we are having a great deal of difficulty holding the amount of bonds that we now have. If a new issue comes along, as it will in December, and we are perhaps trying to roll over our existing holdings which might be among all the banks, perhaps a \$100 million; I do not know, the banks might conceivably be able to buy \$105 million or \$110 million, but to buy a billion or two billion dollars worth is inconceivable. We would have to sell all our other assets which would mean that all other interest rates would go to heaven knows what per cent.

Mr. GRÉGOIRE: What is the meaning of articles 7, 8 and 9. You have mentioned a short term of three years, and there is a mass of short term bond obligations totalling \$3 billion. According to article 8, it is not set for three years; it is set for a period of three months. These \$3 billion worth of short term bonds in three years might be worth \$3 billion but they are not all renewable during the same three months. It would be then just a part of these three months. In calculating the average, it is not stated here that you have to include the returns of American bonds as well as Canadian bonds, just the Canadian bonds that you have.

(Translation)

The CHAIRMAN: I will allow Mr. MacIntosh to give his answer, after which I will stop till 8 o'clock.

(English)

Mr. MACINTOSH: Mr. Gregoire, it would not be simply a question of buying those issues which matured within any given three month period because the opportunity to buy securities occurs seldom; it does not simply arise when new issues are offered by the government. It rises at any moment when you bid or offer in the market and, therefore, it would not simply be a question of new issues. If we raised our price so that we were now buying bonds at  $4\frac{1}{2}$  per cent I assure you we would buy  $\$3\frac{1}{2}$  billion worth of bonds as fast as people could get them into to us.

Mr. GRÉGOIRE: Yes, but you are not obliged to buy those.

The CHAIRMAN: Have you completed your answer, Mr. MacIntosh?

Mr. MACINTOSH: I have finished, sir.

The CHAIRMAN: The meeting is recessed until eight o'clock this evening.

#### EVENING SITTING

The CHAIRMAN: Gentlemen, we will resume our recessed sitting. At this stage it will be on an unofficial basis, with the usual reservations as to no votes being taken, and so on, until it can become official.

When we recessed we had completed a particular round of questioning because we had recognized not only the formal members of the Committee who wanted to be heard, but also the other members participating in our work.

We are still on the question of interest rates and I would ask the members of the Committee present to signify whether they would like to ask further questions on this point, and if so to raise their hands. I want to make sure that those present are aware of the opportunity.

Mr. LIND: Mr. Chairman, what subject are you limiting us to?

The CHAIRMAN: Interest rates.

Mr. LIND: Just interest rates?

The CHAIRMAN: It is a very broad area, as we found out today. I recognize Mr. Gilbert, followed by Dr. McLean and Mr. Lind. Mr. Gilbert, would you like to begin?

Mr. GILBERT: Mr. Chairman, I would like to ask Mr. Paton or Mr. Coleman whether it is possible to set limits on interest rates on the different categories of loans. If we are agreed that the prime interest rate will be charged from six per cent to seven per cent, then is it possible to have upper limits, on consumer loans, mortgage loans and commercial loans? In other words, what would be the effect of setting an upper limit on consumer loans, of 10 or 11 per cent, an upper limit on mortgage loans of eight per cent, and an upper limit on commercial loans of seven or seven and a half per cent, rather than setting the limits on prime loans at seven per cent instead of six per cent as we are doing at the moment?

Mr. PATON: I do not think, Mr. Gilbert, that it would be to the advantage of the country to attempt to apportion certain maximum rates of interest on any particular type of lending. You could get into a discriminatory area if you endeavoured to do that. Under the Small Loans Act, there is an outside ceiling on interest rates that can be charged at present. It is feasible to do this in other areas but not particularly attractive from a practical viewpoint.

When you get into an area of trying to determine maximum interest rates for separate types of lending, then automatically you are making an arbitrary decision in favour on one loan against the other and this, indeed, would lead to further proliferation of such limits. I feel that it would be preferable to let the market control interest rates on any type of lending, subject to the legal limitations regarding usury to prevent getting into an excessive rate. I think that the market should control the going price in any area of lending.

For example, there are many institutions involved in mortgage lending; and if the banking group were inclined to quote excessive rates on mortgages, then they would find very quickly that they would not attract any loans if their competitors were quoting better rates. My inclination would be that this would be a mistake, remembering too that we are legislating for ten years.

Mr. GILBERT: Are you not at the moment categorizing the types of loans that you have at the moment into broad sections such as commercial loans, consumer loans and mortgage loans?

Mr. PATON: We do have categories of loans which are clearly defined, but there is not the variety of rates applicable to these loans. Consumer lending is one; section the rest of our loans another, all on an interest basis subject to the six per cent ceiling.

Mr. GILBERT: The evidence is that the rate on the consumer loans varies between 10 and 11 per cent at the moment, which includes the interest and the service charges. What objection, if any, would you have to imposing a limit of, say, 11 per cent on consumer loans?

Mr. PATON: Eleven per cent is quite a realistic ceiling at the present time. However, since the last revision of the Bank Act we have had prime lending rates on general loans as low as four and a half per cent. In 1954 the prime rate was  $4\frac{1}{2}$  per cent. At that time the 6 per cent ceiling was not too unrealistic, it allowed us  $1\frac{1}{2}$  per cent spread between the risks. But in a very short span of years the 6 per cent ceiling has been completely unrealistic. I would not want to be dogmatic on this, because I would hope that an 11 per cent rate could always be a reasonable rate. But it is possible that it might not be ten years from now.

Mr. GILBERT: An does your same argument apply to commercial and mortgage loans? Mortgage loans at the moment are 8 and  $8\frac{1}{4}$  per cent, which is the highest that I have known them to be in about fifteen years. Are you saying that they might move higher than 8 and  $8\frac{1}{4}$  per cent and, therefore, it would not be wise to impose a limitation on that type of loan?

Mr. PATON: I would not like to try to peer too far into the future to see what the mortgage rate might be, eventually. I think that, legislating as we are for a certain length of time, we would be unwise to endeavour to put a ceiling on mortgage lending and, indeed, on other forms of lending. We might hope that the 8 and  $8\frac{1}{2}$  per cent that we are talking about would be a very adequate ceiling, but once again we get back to the fact that these interest rates are not dictated solely by our Canadian economy. This is a world-wide situation. An 8 per cent mortgage rate in some of the European countries would be a very low rate today in comparison with the rates under which they are working at present.

We should rely basically, as I mentioned earlier, on competition keeping a factual floor and ceiling on lending rates.



Mr. GILBERT: Mr. Paton, the Small Loans Act does not define interest, but the "definition" section defines "cost of the loan". That definition includes all possible costs that may be applicable to a loan. Is that approach feasible with respect to the types of loans that banks have? In other words, if we defined the "cost of a loan" to include all the things that Mr. Coleman listed with regard to bank charges, and applied it to the different types of accounts, is it possible that such a definition would be acceptable to the banks?

Mr. PATON: I doubt that it is feasible.

Mr. GILBERT: Why do you say that, Mr. Paton?

Mr. PATON: You are associating under one heading the cost of different services not related to the lending function if you refer to the service charges against the operating account which Mr. Coleman covered this morning. Anything is possible. It is possible that this could be done, but I do not think it would be realistic to do it.

Mr. GILBERT: I understand that it works out fairly well with the Small Loans Act.

Mr. PATON: It would also in consumer financing. As we mentioned earlier, we would be quite prepared to produce the cost per annum on an interest rate basis for that particular type of lending, but that is a special type of lending. That service charge is an actual cost for the administering of that loan which, presumably, could have 36 payments—they go as long as three years—as opposed to an ordinary revolving loan of a business account of any size, be it \$50,000, \$500,000 or \$5 million.

Mr. McLEAN (*Charlotte*): From what I have heard, being here, it seems to me that the banks object to rigidity, that they are not free to work. It seems that banks are run by management; they are not run by any particular people. And, in fact, they are run for the shareholders. The present rate certainly has a rigidity to it. If a man of good character and in good standing applies for a loan, no matter what kind, I think that he would be looked on more favourably than someone who did not have those qualities. It seems to me that the banks are confined to a degree of rigidity in their operations and they cannot operate as management. Is that so?

Mr. PATON: That is correct. Management does not have the freedom of operation that we would desire to do the job we think is required.

Mr. McLEAN (*Charlotte*): I have heard a lot about this, that and the other thing, but the shareholders have not been mentioned. These are the people who put up the money with the banks and they expect a profit from it—not a big profit, but they expect a safe profit. As I said the ceiling on interest rates places the banks in a rigid position, and I think this should be taken into consideration.

Recently a financier in the United States was asked why he had a certain success and he said it was because of his flexibility of mind. So, it seems to me that the banks need some flexibility in their rigidity because they are not getting this at the present time.

In your opinion, is this change in the issuing of shares, which is related to the capital and reserves, a restrictive thing which is going to be removed? If so is it going to be of any benefit to the banks or to the public?

Mr. PATON: You are referring to the change that is going to take place.

Mr. McLEAN (*Charlotte*): Yes, it is going to be changed and I would like to know your position in the matter.

Mr. PATON: This meets with our approval; this was included in the recommendations that we made.

Mr. McLEAN (*Charlotte*): This meets with your approval?

Mr. PATON: Yes.

Mr. McLEAN (*Charlotte*): Then the shares they are going to issue and the price at which they will be issued will be in the hands of the management of the bank.

Mr. PATON: That would be the effect of Bill C-222.

Mr. McLEAN (*Charlotte*): At the present time the act is restrictive.

Mr. PATON: That is correct, sir. Perhaps I should amend that: restrictive as to price.

Mr. McLEAN (*Charlotte*): The price of the shares.

Mr. PATON: There is no restriction on us so far as issuing shares is concerned either than the issue price.

Mr. McLEAN (*Charlotte*): Oh, no. The price of the shares is restricted at the present time; it relates to your capital and reserves, and you cannot do anything about it. You could issue them for more or less if the new act goes through?

Mr. PATON: That is right.

Mr. McLEAN (*Charlotte*): There always has been a restriction on banks lending on bank stock?

Mr. PATON: Yes, sir.

Mr. McLEAN (*Charlotte*): Why would there be any reason at the present time for the banks lending on bank stock if only 10 per cent—no matter what combination you used—could buy only 10 per cent of the bank's stocks? Should the banks not lend on bank stock as well as on any other security?

Mr. PATON: I would say that we are not unhappy with that restriction.

Mr. McLEAN (*Charlotte*): I know, but the general public might be unhappy. If certain people own bank stock, want a loan, go into the bank, they cannot get it because it is bank stock. Why should it be restricted to bank stock when you could not possibly buy control of a bank. You could do this before but you could not possibly buy it now because you are restricted to 10 per cent.

Mr. PATON: If the banks were permitted to lend against the security of its own shares, notwithstanding the 10 per cent restriction, there could be a situation wherein they could have quite a substantial volume of loans out against them.

Mr. McLEAN (*Charlotte*): The general public own the bank stock but yet someone could go into a bank, not necessarily the same bank, and say: "Look, I have this bank stock but I cannot get a loan." I do not think that is right. I think anyone owning bank stock should be able to get a loan on it just the same as on any other stock.

The CHAIRMAN: Mr. Elderkin, can you give us some of the reasons for this?

Mr. C. F. ELDERKIN (*Inspector General of Banks*): This has been in the act almost since Confederation.

Mr. McLEAN (*Charlotte*): Yes, but the restrictions are not in effect until this act is passed. These are restrictions as to ownership and the amount of ownership.

Mr. ELDERKIN: But only the amount of ownership of one individual. You could have a dozen or more individuals and you will have more who own bank stock in the same bank. I think it would be very undesirable.

Mr. McLEAN (*Charlotte*): That puts a restriction on the general public buying bank stocks.

Mr. ELDERKIN: There is no restriction on buying bank stocks.

Mr. McLEAN (*Charlotte*): But if they buy bank stock they are taking a risk in that if they need money at some time they are not able to borrow it. So you would not rely on bank stock perhaps in the same way as you would on another stock. I think bank stocks are the best stocks in the world, but you could not borrow on them if you get hard up.

I think that is all I have to say.

The CHAIRMAN: Thank you, Mr. McLean. Mr. Fulton, we are still on the broad area of interest rates. Have you a question.

Mr. FULTON: Mr. Chairman, I think the situation is as it was the last time you asked me. My questions do not relate specifically to the interest rates or to anything in the submission made by the Bankers' Association. I have a series of general questions on matters relating to the bill. I would be quite prepared to pass if you would call on me later.

The CHAIRMAN: I will try to indicate to you privately when we review the topics raised by the bankers in their submission. We might be able to have a round of questions at that time on any matters we have not discussed.

Mr. FULTON: For instance, I would like to follow up the subject which was being discussed when I was questioning earlier, the matter of the reserves required to be held with the Bank of Canada, the interest on those reserves and following on from there. I think I could relate it to something under discussion.

The CHAIRMAN: I believe there is a section on the question of reserve requirements in the banks.

Mr. FULTON: Yes, but if you want to complete the interest rate matter, I must hold my questions over until we reach a related subject.

The CHAIRMAN: I think the Committee felt this would be the useful approach, because, our discussions would be more useful. I will recognize you this evening if you want to ask questions.

Mr. FULTON: Yes, if we finish the interest rate matter this evening.

The CHAIRMAN: Mr. Paton, you have some information with reference to questions raised by Mr. Laflamme and Mr. Clermont.

Mr. PATON: Yes, I have, Mr. Chairman. I was asked would it be possible for us to attach a name to each of the banks on the list which we distributed to the Committee covering the charges on the personal loans, designated at the moment as banks A, B, C, D, E, and so on.



The CHAIRMAN: I actually made the request arising from questions asked by our colleagues.

Mr. PATON: I suggested I would like to take it under advisement and check with my group. I now have the information and I will be very glad to relate it to the Committee. I should point out that these rates or charges are those which were in effect at the beginning of November but the banks, operating in their customary competitive manner, are at liberty to change these at any time.

The CHAIRMAN: Perhaps more favourably.

Mr. PATON: More favourable either to the borrower or to the banks.

The CHAIRMAN: I had the borrower in mind.

Mr. PATON: If you like I will recite them to you. Bank A is the Bank of Montreal; Bank B is the Bank of Nova Scotia; Bank C is the Toronto Dominion Bank; Bank D is the La Banque Provinciale du Canada; Bank E is the Canadian Imperial Bank of Commerce; Bank F is the Royal Bank of Canada; Bank G is the Banque Canadienne Nationale, and Bank H is the Mercantile Bank of Canada.

The CHAIRMAN: Thank you very much. Perhaps the Committee should reproduce these and distribute them around the country. I think that for some time now we have been in a position to make our session more formal. I would like a motion to that effect.

Mr. CLERMONT: I so move.

Mr. LAFLAMME: I second the motion.

Motion agreed to.

The CHAIRMAN: Mr. Clermont, did you indicate that you wanted to be recognized again while we are in the area of interest rates?

Mr. CLERMONT: No, not on interest rates.

The CHAIRMAN: You are not interested in interest rates at this point.

Mr. CLERMONT: Would you consider competition under that subject?

The CHAIRMAN: Competition between the banks on interest rates?

Mr. CLERMONT: No, the competition between banks and near-banks.

The CHAIRMAN: If you can relate your questions to the general topic of interest rates, we would be happy to have them.

Mr. CLERMONT: I would prefer to come after the others.

The CHAIRMAN: All right. Mr. Wahn, would you proceed?

Mr. WAHN: Mr. Paton, I gather from the brief that in your view and in the view of your association, because of the general rise that is taking place in interest rates in Canada, the 6 per cent ceiling is unrealistic.

Mr. PATON: That is correct.

Mr. WAHN: I understand, the bill will permit the banks to charge up to 7 per cent.

Mr. PATON: We arrived this afternoon at a figure of  $7\frac{1}{4}$  per cent as of January 1st, assuming that this legislation has been passed by then.

Mr. WAHN: And although that may not be as satisfactory as you would like, it obviously is an improvement upon the present position.

Mr. PATON: Correct.

Mr. WAHN: The brief, as I understand it, suggested that the ceiling should be removed completely. Either you or one of the other witnesses indicated, in reply to a question, that if the ceiling were removed entirely, the competition among lending institutions would be sufficient to keep lending rates reasonable. Would you agree with that proposition?

Mr. PATON: I would agree with that.

Mr. WAHN: Putting it another way, would it be fair to say that you would agree that, for the protection of the Canadian public, interest rates must be regulated in some way; if they are not regulated by a public authority then they must be regulated by effective competition.

Mr. PATON: That is correct.

Mr. WAHN: My recollection from reading the Porter Report is that it was felt that at the present time more competition was required in the banking industry. I gather your association is in agreement with that?

Mr. PATON: That is right.

Mr. WAHN: Assuming that to be true, is it not bound to take some little time before you can move from a state of imperfect competition, with regard to bank lending rates, to a state of full and effective price competition? Would it not be unusual to expect that with the mere stroke of a legislative pen the present imperfect competition, which I gather exists in the banking field, is suddenly converted over night into perfect and effective competition?

Mr. PATON: I would agree sir, that it would take some time to recognize the changed status.

Mr. WAHN: Is it not a fact that at the present time there is a great shortage of capital not only in Canada but around the world?

Mr. PATON: That is correct. Tight money is in effect.

Mr. WAHN: And that is general throughout the world, particularly with capital funds. We have Europeans coming over here to try to raise loans.

Is it also true that when anything is in short supply, competition is not likely to be as effective as when that particular commodity or article is in good supply? To take two specific examples, if rental housing is in very short supply, rental rates are likely to become unreasonable unless the government maintains some control; if there is a shortage of sugar, sugar prices are likely to go up very high unless controls are imposed. Is it not a general, almost a common sense principle, that when any commodity is in short supply, competition is not likely to be a very effective regulator of rates until supplies become more normal?

Mr. PATON: I do not necessarily think so, Mr. Wahn. I think competition would be just as effective, provided all participants in the field are operating with the same freedom. I think that with fuller participation by more people, it could result in the reverse.

Mr. WAHN: Let me put it to you this way. Would you not agree that if capital were in greater supply than it is now, that competition among banking institutions would be even more effective than it is likely to be when capital is in very short supply—"Effective" not in the sense of measurement accomplished but effective in keeping lending rates at a reasonable level or lower?

Mr. PATON: As we all know, the effect of the law of supply and demand, is involved in this whole question of the level of rates.

The CHAIRMAN: Mr. Paton, if money is a commodity like other commodities, as Mr. Coleman suggested this morning, why would the behaviour of money as a commodity be any different than the commodity of sugar, to which Mr. Wahn referred?

Mr. FULTON: Did Mr. Coleman really suggest that money as a commodity was like other commodities?

The CHAIRMAN: Yes.

Mr. FULTON: Sugar is not controlled by the Bank of Canada so how can money be a commodity like sugar? Perhaps it is a commodity, but surely it is not a commodity like other commodities when it is controlled by the Bank of Canada.

Mr. COLEMAN: I just forget the exact context in which that answer was given. What I was trying to explain at the time was that naturally when there is not a shortage—and I think this is what Mr. Wahn is trying to point out—of, say, sugar—and I mentioned sugar—the price goes down, and when money is free you compete at a lower level. I was just saying that money in that respect is no different from the standpoint of supply and demand.

Mr. FULTON: I agree but I would hesitate to agree to the general proposition that money is a commodity like others.

Mr. COLEMAN: I did not intend that. I was trying to give an example of supply and demand.

Mr. FULTON: I was sure you had not said it in that way.

Mr. COLEMAN: I did refer to it.

The CHAIRMAN: I do not think you had yet arrived when the comment was made. I am not trying to create a controversy but I think Mr. Coleman will agree that he had made some reference to money being a commodity—

Mr. COLEMAN: I did.

The CHAIRMAN: —during the explanation of interest rates and so on.

Mr. COLEMAN: Yes, that is right.

Mr. WAHN: The general point I was trying to make is that I believe it is unrealistic at a time when money is in very short supply and in great demand to expect that competition will be truly effective in keeping rates low. It is our invariable experience that when commodities get into short supply the government often has to step in to regulate the price, if they are vital commodities. For example, this happened during the last war. The reason, of course, is that competition does not become effective in those circumstances.

Mr. Paton, I understand the legislation will remove the ceiling entirely once interest rates on short term government bonds decline to a more normal level—I do not know just what the percentage is, but it is around  $4\frac{1}{2}$  per cent—the ceiling on chartered bank interest rates will be removed completely. Is it not fair to say that when that happy time arrives—and it may be some time—when interest rates have fallen back to a more usual level, that competition is likely to be much more effective in reducing bank interest rates than it would be at the present time.



Mr. PATON: Mr. Wahn, I think we are looking for competition among the entire financial system, our ability to enter into the entire financial system on a free basis, and on a basis more compatible with the others. This would thereby bring larger participation into this financial community which might well have the effect, if not of reducing interest rates, certainly keeping the average interest rates at a lower level than otherwise would exist. I cannot quarrel with your thesis on rental houses that are in short supply, and rents going up and so on. But the area that we are concerned about is that of permitting us to get into this bracket from which we are presently excluded, thereby, we feel, benefiting the over-all financial context of the whole community.

Mr. WAHN: My point perhaps is rather than urging the government to remove the ceiling altogether at a time when there is a general world wide shortage of capital, in view of the factors which I have mentioned, that it would have been more reasonable for the association to have requested the ceiling be removed when perhaps interest rates declined not quite as much as is required by the present legislation; in other words, make the cut-off earlier, if it is anticipated, as I understand it is, that it may be some time before interest rates on short term government bonds do decline to  $4\frac{1}{2}$  per cent, when you may end up with a ceiling on for some considerable time. But at a time of a world wide shortage of capital, and at a time when we have been told by the Porter Commission that there is lack of competition—it may take a little while for the competition to become effective—I would have thought that you would have to agree to taking off your bankers association hat and putting on the hat of an ordinary Canadian citizen, and to agree that perhaps the government is being reasonable in raising the ceiling to slightly over 7 per cent, but not doing away with it entirely until money comes into better supply.

Mr. PATON: I would suggest, Mr. Wahn, that probably a better time to have the ceiling removed would be when the interest level is high, which is probably the reverse of what you are suggesting. I think the ability to compete for the savings, which presently may well be channelled into other sources, is important. I am not excluding the near-banks, but I am not only thinking of the near-banks. Under current conditions this disability is contributing to the present tightness more so than if the banks currently were able to compete for these funds. This would attract an increasing amount which would thereby enable them to satisfy to a better extent the very heavy loan demand.

Mr. WAHN: It is difficult to see how that would increase the over-all savings which are available for lending purposes. You may attract some from the trust companies or the loan associations, but it is difficult to see how you are going to increase the over-all amount. I gather from the Porter Commission report that the rate of savings remains reasonably constant. There may be a shifting between the banks and the other companies, but you are not going to increase the over-all rate of savings by—

Mr. PATON: The point we made earlier today basically is that this release from the interest ceiling would permit us to get into an area of lending that is presently paying a high cost. This would have the effect, as we pointed out this morning, of these borrowers in this area coming under the umbrella of bank lending at a rate lower than they currently are paying. This is one of the points that we have made in our brief. The Porter Commission, I think, made it, and we think that this is a real point.

Mr. WAHN: There is really only one other question I have, Mr. Chairman. A statement appears on page 1 of the submission of the Canadian Bankers' Association:

At the same time, other financial institutions have moved increasingly into what is essentially banking business.

Mr. Paton, has it not always been considered that one of the basic job of the bank is to provide business with short term money for operating purposes rather than long term money? This is essentially what banking business is on the lending side. What other institutions are moving into that aspect of banking activity?

Mr. PATON: You are referring to institutions getting into the working capital area for businesses?

Mr. WAHN: That is essentially banking business. Really that is your basic business.

Mr. PATON: One area is the finance companies that have become much more actively employed in advancing funds to the business community, generally against fixed assets owned by the business, which are used by the proprietor for working capital. Mr. Coleman, have you any others? This is in the lending business and I am getting a lot of support from my colleagues behind here. You were referring solely to the lending end of our operations?

Mr. WAHN: Yes, because that is what we are concerned about. This ties in again, of course, with the raising but maintaining the bank ceiling until such time as competitive conditions do prevail in the banking business.

Mr. PATON: Basically you cannot separate the two because other institutions have gone into a deposit gathering business to a substantially greater extent which, in turn, hampers and has hampered our ability to lend over the last decade.

Mr. WAHN: But I am thinking from the point of view of public interest distinct from the interest of the bank. They do not always coincide although I realize that they generally do—and they do not always coincide perfectly or exactly. From the point of view of the public interest it is essential that there should be effective competition in the essential business of banking which is, as I have always understood it, the lending of money to businesses for short term operating requirements. I cannot think of any, with the possible exception of the finance companies who really have a slightly different type of operation, that are moving into that particular banking field. Is that not another reason that perhaps the government is wise in not providing for an immediate removal of the ceiling but, instead, providing that it will be removed when interest rates decline to a more normal level—and that presumably indicates that capital again is in somewhat better supply.

Mr. PATON: I do not think you can separate the lending function of the banking business from the gathering of deposits. You must join the two of them together, Mr. Wahn, because one cannot be done without the other. This is where the competition has been basically inequitable in so far as the banks are concerned, thereby limiting their ability to make these loans, which, you say, are essentially our prime area of business. Mr. Coleman might like to supplement.

Mr. COLEMAN: Mr. Wahn, I think a good example where other institutions have moved into what has been heretofore regarded as essentially banking business is other non-bank institutions providing facilities for checking accounts, savings accounts—and they are not prohibited or inhibited in any way from going out and bidding for these deposits, they are able to pay higher interest rates because there is no ceiling on the amount they can charge for loans. This is why, as the Governor of the Bank of Canada pointed out in his evidence, that an increasingly larger share is being taken by these non-bank financial institutions all the time. The bank's growth does not compare favourably with these other institutions that are not competing under the same rules that we compete under. We have no objection to competition but we think we should all play under the same rules. That is not the situation today.

Mr. WAHN: That is all I have, Mr. Chairman.

Mr. LAFLAMME: May I ask you some related questions in this field.

The CHAIRMAN: Mr. Laflamme, you ask your supplementary question and then I will recognize Mr. Latulippe, followed by Mr. Cameron, yourself, and Mr. McLean.

Mr. LAFLAMME: Mr. Coleman, is it not a fact that the main effect of more competition between banks and other financial institutions will be to decrease the average level of interest rates charged by those financial institutions, although it will not decrease at all the interest rates of chartered banks.

Mr. COLEMAN: Mr. Laflamme, if I understand your question correctly, you are suggesting that if the banks are in a more competitive position it would tend to bring the rates down?

Mr. LAFLAMME: The rates of the others.

Mr. COLEMAN: Well, I think that has been proven since the banks have gone into the consumer loan business. You will find that consumer loans on the average cost less today, outside banks, than they did before because of the strong, vigorous competition that the banks have provided in the personal loan field.

Mr. LAFLAMME: Would it not have the effect of increasing the general business of the banks and give more credit control by the Bank of Canada.

Mr. COLEMAN: We would hope that we would recapture at least what we use to regard as a reasonable share. We do not want all the pie but we think with institutions competing, having certain advantages on one side that we do not have, that it is hardly equitable, and we think it reacts seriously to the detriment of the public.

The CHAIRMAN: I will now recognize Mr. Latulippe.

Mr. CLERMONT: Mr. Chairman, when you called my name before I was not ready. Would you put my name on the list.

The CHAIRMAN: We will definitely do that, Mr. Clermont.

*(Translation)*

Mr. LATULIPPE: Would the removal of the ceiling from interest rates, mean a rise in the cost of living, just as the raise in wages is increasing the cost of living? Would these gentlemen admit that?



Mr. LAVOIE: I do not believe so, Mr. Latulippe. I believe that the purpose of removing this ceiling is to allow a category of lenders to borrow money more easily and more cheaply from the bank. This will be better for them than to borrow from other institutions such as a finance company.

Mr. LATULIPPE: That is the unfortunate side of a national economic situation where we see the spread between rich and poor extending. People are facing increasing deficits on the one hand, and others are accumulating surpluses. Even the Governments are getting into larger deficits all the time. Do your banks prefer to lend money over the long term or over the short term?

Mr. LAVOIE: The policy of the chartered banks has always been to lend on short term rather than on long term. The type of loans which we prefer making is a commercial loan, and these are normally short term loans.

Mr. LATULIPPE: Mr. Chairman, I have a little table here. I know nothing about finance or accounting. I know about finances because I have paid interest. I see a table here regarding a loan made, 163 million at 26 percent repaid over 50 years. This costs 449 millions in interest. A 163 million loan means that you have to pay 489 million in interest. I thought you did not want long term loans?

Mr. LAVOIE: Mr. Latulippe, as I mentioned a few moments ago, I believe that the role of the chartered banks is to lend on the short term, normally, at least. I do not believe that the bank's policy normally is to lend on such a long term basis at 50, 60 or 70 years.

Mr. LATULIPPE: This firm is going to bring in over 449 million in interest at 6 percent over 50 years on 163 million to pay 7 million per year. It is going to reimburse 710 million, and after 50 years it is still going to owe 282 million. Is it logical that sums like this should be loaned where the interest multiplies the principal to such a phenomenal extent?

Mr. LAVOIE: I fail to understand your question, Mr. Latulippe. You mentioned a moment ago that the firm in question had about 163 million, and 50 years later it still owed 289 million?

Mr. LATULIPPE: They are going to repay 310 million, and they will still have to pay 289 million after that, because the overall interest at 6 percent costs 489 million.

Mr. LAVOIE: That is a problem which is very difficult to solve. Since I have been working for a bank I have never met with any such case.

Mr. LATULIPPE: The table I have here—

The CHAIRMAN: I would like Mr. Latulippe to figure out his interest himself. I do not think I could get it.

Mr. LATULIPPE: 163 million at 6 per cent for 50 years costs 489 million.

Mr. LAVOIE: Was this at compound interest?

Mr. LATULIPPE: No, not at compound interest, it is simple interest. If it were a compound interest it would be still higher.

The CHAIRMAN: Since banks do not lend on the long term it might be a little difficult for the witness to comment in depth on your question, Mr. Latulippe.

Mr. LATULIPPE: Mr. Chairman, I conclude that the interest on money is absurd and inevitable. I think it is quite against the laws of arithmetic and it is against social welfare, there is certainly a vicious circle in this.

Mr. LAVOIE: I fail to see that a bank could lend money without interest. The bank would have to pay interest to depositors on the sums which it receives in the form of deposits. There is no equilibrium when you lend 163 million and you take in 489 million. I believe that no bank in this country has ever indulged in such a transaction.

Mr. LATULIPPE: Mr. Chairman, the choice is as between stopping development, and making loans. We have to choose between letting people falling into debt or borrowing to increase their debt. There does not seem to be anything we can do to improve this. The debt is quite immeasurable. Interest on money is quite illogical. We get extraordinary sums with this. It is just as I was saying a minute ago, it is illogical, there is no end to it.

The CHAIRMAN: Any comments.

Mr. LAVOIE: What is the meaning of that question?

The CHAIRMAN: I believe Mr. Latulippe has raised an argument which will be more in order when we begin our discussion on the Bill itself, clause by clause. At this point he can offer arguments against the interest rates, however, for the moment, we are asking certain representatives from the chartered banks what is their feeling on the Act we have before us. I feel that it would be a little difficult to ask a representative of a chartered bank to say that interest rates are immoral.

Mr. LATULIPPE: I can agree with that. I will express myself differently if you like. We are far from having anything against the chartered banks. They are good institutions we must keep, they are in business and doing business well. Canada certainly needs these institutions. We are not against the chartered banks, but we want to correct, the errors that there may be in the system; we want to correct any misunderstandings that may have arisen. But if we are discussing these matters in order to correct any errors who is going to bring up these matters if not us? That is why I respectfully draw to your attention the tables and figures in question.

Mr. LAFLAMME: On a point of order, Mr. Chairman. I have, of course, no wish to rush to the defence of the banks, however, speaking as a member of the Committee I would not like to say that what Mr. Latulippe has said is the exact truth. He speaks of a certain amount of money which presumably has been borrowed, and he adds on to that sum the interest rates over 50 years before the 50 years are up, and then he begins to speak of annual equal payments to demonstrate that after 50 years, the eventual amount is larger than the original amount of the loan, which is quite impossible.

Mr. LATULIPPE: It is clear that my figures are correct.

The CHAIRMAN: I would not like to prevent you from putting before the Committee any ideas which you might have. The Committee, I think, might look at Mr. Laflamme's ideas as well as at Mr. Latulippe's. I do not think we have to ask our witness exactly what he feels about it or to help us out in this debate. Now I believe I can give the floor to Mr. Cameron.

(English)

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Chairman, I would like to pursue this question of competition again.

I was interested in Mr. Lavoie's suggestion that the lifting of the ceiling on interest rates would enable the banks to lend money in areas in which they have not hitherto been able to lend and that this would be to the advantage of the borrowing public. I can think of a number of reasons the 6 per cent ceiling should be lifted but they have nothing to do with this. I am just wondering whether there is any way in which you can substantiate the proposition that when the 6 per cent ceiling is lifted you will be able to lend money to people at more advantageous rates than those who are now lending through the near-banks system. I think that has to be proved. In fact, I cannot quite see how you can do so unless you are prepared to narrow the margin between what you have to pay and what you are going to get.

I remember some few years ago, when we were investigating the small loan companies—and I believe the situation has changed somewhat since then—the vast bulk of the funds that was being retailed, shall I say, by the small loan companies was being wholesaled by the chartered banks to them. Evidence we had from some of them showed about 75 to 80 per cent of the funds were in the nature of bank loans. No one presumed that they made their money on the margin, between what they paid the chartered banks and what they charged the public. It seems to me the same position is going to obtain now; we are going to take the ceiling off, which will enable you to pay more for deposits, and if you are successful, you will be able then, presumably, to attract deposits that otherwise would go to the near-banks. I would like some evidence that this will result in cheaper loans for the general public than they are getting from the near-banks—and why this should be so.

I do not think that you should base your argument for the removal of the 6 per cent ceiling on what seems to me extremely shaky grounds. I would like to know what the evidence is support the contention that you will be able to work to the advantage of the borrowing public and lend the money really at cheaper rates than the near-banks are doing now.

Mr. COLEMAN: Well, Mr. Cameron, there is a large segment of the population that today are not able to borrow from the banks because the risk is not a 6 per cent risk; it might be a 7 or an 8 per cent risk in the eyes of the bank. Quite possibly today, those people are paying between 8 and 18 per cent. I think a good analogy would be personal loans. Since the banks have gone into the personal loan field—and this was just mentioned a minute ago—the general rate has gone down. The borrowing public today, borrowing from the banks on consumer loans, are getting those loans at rates probably up to half of what they were paying before. Although the rates will vary with different companies; I think this is perhaps the best example I can give you.

The CHAIRMAN: Sir, did I hear you say a large segment of the public?

Mr. COLEMAN: I would say there is quite a substantial segment. Would you like me to give an example?

The CHAIRMAN: I was going to ask, with Mr. Cameron's permission, whether you could define the size of that magnitude compared with the size of the magnitude of the public that is already borrowing from you—in other words, the customers?



Mr. COLEMAN: I would not be able to be that specific, Mr. Chairman. Let me take a man who has a fleet of trucks hauling gravel or something like that. Today that is not a 6 per cent risk. If this bill goes through we will be able to take security on his equipment, which we cannot do today; and if we are freed from an interest rate ceiling we could probably make that loan, thinking of today's cost of money at  $7\frac{1}{2}$  or 8 per cent, I would guess that that man is paying anything up to—well you name it; it could be 18 per cent.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You say he is paying 18 per cent if he is giving as security his equipment?

Mr. COLEMAN: Yes, I do.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Is not the important factor in your being able to lower the rates the fact that you will be able to take as security a lien on his equipment?

Mr. COLEMAN: No, I think it is the quality of the risk, Mr. Cameron, as well. It is the quality of the risk plus the feature that we will be able to take security.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I would like a definition of your term "quality of risk". I can understand that I would be a much better risk if I came into your bank with a bundle of Government of Canada bonds and asked for a loan than if I came in merely with my smiling face. I want to know how you evaluate this except on these very practical terms of what you can put up as security?

Mr. COLEMAN: Well, in the example you gave, you know you would pay the same interest rate whether you had bonds or just had a smile.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, you would charge me as much if I had the bonds.

Mr. COLEMAN: Today, because what is happening is that the minimum has become the maximum. I do not think anyone could successfully argue that competition does not bring costs down. You can take an example in a small town. If you have one car dealer selling used cars, the chances are he will get a better price than if there were five others selling them.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Now, just wait a minute. Let me revert to this question of competition. The only place I can see where competition comes into it is between the banks themselves, to attract deposits. Certainly at the present time this competition is among would-be borrowers.

Mr. COLEMAN: Are you suggesting there is not competition in the banks for borrowers?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I would suggest that they do not have to compete very hard in conditions of tight money.

Mr. COLEMAN: I think so far as the small borrower is concerned he has not suffered in this tight money period. There is great competition for this business today by our bank and I think this applies to the other banks. We have tried to ensure that the small borrower has been looked after in this period of tight money. I would doubt if you could find a creditworthy person who has gone into any bank and has been turned down for a small loan.

An hon. MEMBER: A personal loan?

Mr. COLEMAN: I am talking about consumer loans, small loans.

Mr. FULTON: This does not apply to commercial loans because you cannot take security. For that reason he is driven to the institutions where he is paying as you say, from 8 to 18 per cent.

Mr. COLEMAN: I am referring to someone who is creditworthy, who is entitled to a loan, and I say there is competition for that business today.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, small borrowers. Apart from your public-spiritedness and so on, why is there competition for this particular type of loan?

Mr. COLEMAN: Well, we want to look after the public and we also want to make a profit.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I would like to know why these are particularly desirable from the profit making point of view?

Mr. COLEMAN: Because there is a spread.

An hon. MEMBER: Greed.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Ah!

Mr. COLEMAN: There is a spread and it provides a profit margin.

Mr. FULTON: I have a supplementary. A while ago, you were discussing the features which would enable the small commercial borrower to borrow from the banks at lower rates than they now have to pay, and you said that if the banks were allowed, as they will be now, to take security on this equipment—you were referring to his gravel truck—

Mr. COLEMAN: That is right.

Mr. FULTON: —then he would be able to get a loan from you at lower rates than he is, in general, now paying. Is there not another feature which you did not mention as to why he would be able to come to the bank and get it at perhaps 8½ per cent. Mr. Cameron questioned whether you would lend it to him at 8½ per cent if other people were charging up to 18 per cent. Is not one of the reasons that you would be able to do that, and would do that, is because this would be a comparatively small segment of the banks' business. In other words, this might be a risk for which others feel justified in charging up to 18 per cent. So long as you think he is reasonably creditworthy can you not take some risk and lend it to him at 8 per cent or 8½ per cent?

Mr. COLEMAN: That is right.

Mr. FULTON: But if this was the only kind of business you were doing you would probably charge 18 per cent.

Mr. COLEMAN: Well, I go along with you right up to the last three or four words, Mr. Fulton, but I just have to think that over.

Mr. FULTON: Well, do you not in the overall banking policy sort of average out your risk?

The CHAIRMAN: In fairness to Mr. Coleman, I believe that earlier today, in answer to similar questions he said that they did not.

Mr. COLEMAN: I am not sure what you mean by averaging out a risk, Mr. Fulton.

Mr. FULTON: If I was the only customer you had, to reduce it to an absurdity, you would probably have to charge a higher rate to make certain of

your position than if my business was but a fraction of the over-all business you were doing.

Mr. COLEMAN: You mean if the loss was spread all over the country?

Mr. FULTON: Yes.

Mr. COLEMAN: That is true.

Mr. FULTON: Because you have a large amount of certain well secured loans you would, looking at your whole meld of business be able to say; "O.K. We can take this one on at 8 per cent," I am not saying you are foolish or reckless, and if you lose on this type of business it is not going to drive you bankrupt.

Mr. COLEMAN: Yes, I think that is right.

Mr. FULTON: Is letting the banks into this field going to benefit everybody who is looking for this type of loan.

Mr. COLEMAN: We think so.

Mr. FULTON: That is the point I was trying to make. I did not make it very well.

Mr. COLEMAN: Mr. Cameron, I answered your question.

The CHAIRMAN: Mr. Fulton, I had understood Mr. Coleman to tell one of our members earlier today that if the bank went into riskier lines of business, if these provisions were adopted, they still would not expect their present customers to, in effect, subsidize the risk. I forget which one of our members introduced that line of questioning, I do not think that I am totally incorrect in the way I have summarized it.

Mr. PATON: I think your summary is correct with regard to the concept within which it was said, Mr. Chairman, but our basic responsibility is to continue to look after the type of lending that we have been doing and are doing. You might say we have an involuntary averaging out of our risk because we have some 5700 branch managers at the moment across the country and one man's conception of a good risk differs greatly from another's. We have various qualities of lending abilities throughout the service and we are faced with an involuntary average.

Mr. FULTON: I have to come back to the last couple of exchanges and to Mr. Cameron's question: Why would you lend it at 8 per cent if the others are getting 18 per cent?

Mr. PATON: Why would we lend it at 8 per cent?

Mr. FULTON: Yes, if the others are charging 18 per cent and are taking security.

Mr. PATON: We are satisfied, Mr. Fulton, that we would be able to lend at considerably lower rates than the going rate. The range of figures from 8 to 18 is perhaps unfortunate because we do not really know; we cannot put a figure on what a risk would be presently paying. But we do know, however, by our participation in lending and with the knowledge of lending that we have through many years of experience, that we could handle this type of loan, that Mr. Coleman referred to, at a rate of interest which would be within reasonable compass of the best rate. Assuming that the prime rate was 6 to 6½ under current conditions, an 8 to 8½ per cent risk would be something that would be quite within our standard of credit.



Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): May I carry on from that point, Mr. Paton? I would hate to inject a note of cynicism into it, but what would induce you to charge rates any lower than is necessary for you to attract that business from the present small loan lenders?

Mr. PATON: Mr. Cameron, we are going to be in business for a long while; we have been, and we hope to continue. Our philosophy all through history has been to provide for a reasonable spread no matter how the economy is. Whether you have a low prime rate or a high prime rate, our philosophy has been this, and I know of no reason at all for changing this philosophy, assuming that the prime rate is removed.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I must point out to you, Mr. Paton, that you have had no option up until now—

Mr. PATON: Yes, we have had.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): —within the limits of the ceiling?

Mr. PATON: We had a ceiling of 7 per cent at one time, and at the time there was a 7 per cent ceiling we had a prime rate of  $4\frac{1}{2}$ . Now, had we been so inclined to try to charge the full amount the traffic would bear, our prime rate would not have been  $4\frac{1}{2}$ .

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I notice, however, Mr. Paton, that as soon as the traffic did bear it, in fact as soon as money got tight, you apparently came right up to the limit of the ceiling.

Mr. PATON: Not immediately, sir. We have a table showing how the prime rate has moved in the last 20 years, and if you look at it you will find that it has moved from  $4\frac{1}{2}$  to  $5\frac{1}{4}$ , to  $5\frac{1}{2}$ .

Mr. COLEMAN: In the normal course of events, Mr. Cameron, competition should take care of this.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Competition on the part of whom?

Mr. COLEMAN: Everyone who is lending money. Competition should, in a normal course, take care of this, and the rates charged should reach a level—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I agree that there must be competition, Mr. Coleman, if the banks are having difficulty in placing loans. But you have repeatedly told us that we have a tight money situation, which would seem to indicate that that is not the situation now.

Mr. COLEMAN: Yes, we are in an unusually tight money period.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Do you foresee a relaxation of that tight money situation in the foreseeable future, in view of the admitted shortage of capital throughout the world?

Mr. COLEMAN: I am not an expert in this field, Mr. Cameron, but for what it is worth, I do not see interest rates going down in the reasonably near future.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): So, we shall always be in this position. Is your argument about having to compete for suitable placements for loans valid in these circumstances?

Mr. COLEMAN: Well, if we are able to attract more deposits by being able to compete, we should have more money to lend.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): That is the point. The competition is in the attracting of deposits then?

Mr. COLEMAN: And if we have more money to lend it will be in the search for suitable loans too.

Mr. PATON: These borrowers, Mr. Cameron, will become depositors; if not right away, they will develop as depositors. As I say, we are in business for a long time and, therefore, we will benefit from the change in their financial condition. As they progress, we will progress.

Mr. LAMBERT: As an observation, would you not rather loan to a man three times at 8 per cent than once at 18 per cent? This is repeat business. This is what you want. Every time a man comes into the bank there is a chance of some more business.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I thought that he had to come three times at 18 per cent.

The CHAIRMAN: He can be bled only once. Would you accept a further supplementary question from Mr. Lind?

Mr. LIND: Due to the fact that the banks can borrow money much cheaper than the near-banks—the trust companies, the loan companies and the finance companies mostly borrow from the banks—is it not a fact that you can borrow from the general public by deposits at  $1\frac{1}{2}$  to 2 per cent cheaper than maybe some of the other institutions?

Mr. PATON: We are competing in a market, Mr. Lind. I think you must remember that we gather large quantities of funds in very small units. Our bank system, all through the piece, accumulates deposits which are expensive to gather. We have branch facilities; we have vault facilities and the usual accoutrements that are necessary for opening a bank. The major part of our funds do not come from going out onto the money market and bidding on large amounts. The millions of dollars in savings deposits that we have generate right across the country, as you are well aware, and these are expensive amounts to gather in, in relation to the overhead that we have to bear.

On the other end of our funds, are the short term market funds for which near banks and finance companies are competing currently, and have done so since 1954, bearing in mind that every controller of corporations, who, is, I would say, worthy of the name, is utilizing his spare funds to a far greater extent than he did in former years. These amounts are relatively easy to gather from a cost angle, apart from the actual interest rate that is paid. Now, in this area, we currently are just not in the ball park at all.

The CHAIRMAN: But you still have 70 per cent of the deposits.

Mr. PATON: I think the governor used a figure of 73 per cent. However, he was relating this to the near-banks. If you relate the percentage of savings deposits that the banks have to all savings institutions—life insurance companies, trust and pension funds, which are competitive saving depositories, no matter what you call them because they are competing for public savings—you will find that our percentage is closer to 25 per cent.

The CHAIRMAN: You are not competing with the insurance companies and pension funds in exactly the same way as you are competing with the trust companies.

Mr. PATON: Not in exactly the same way, Mr. Chairman, but every bit as effectively. The Canada Savings Bonds is another source of direct competition, although a worthy competition, with our bank savings. I think we should keep that ratio equally in mind as well as the 73 per cent which the governor used quite correctly in the comparisons which he made.

Mr. WAHN: May I ask another question, Mr. Chairman?

Mr. PATON: I have these prime rates that I suggested I might give. Would you be interested in hearing them?

An hon. MEMBER: Yes.

Mr. PATON: In December of 1944 the prime rate was  $4\frac{1}{2}$  and it stayed at  $4\frac{1}{2}$  until April, 1956 when it went up to 5 per cent. On August 20, 1956 it went up to  $5\frac{1}{4}$ ; in October it went up to  $5\frac{1}{2}$ ; in August, 1957 it went up to  $5\frac{3}{4}$ ; in December, 1957 the rate went down to  $5\frac{1}{2}$ ; in February, 1958 down to  $5\frac{1}{4}$ ; in 1959 back to  $5\frac{1}{2}$ ; up to  $5\frac{3}{4}$  in April, 1959 and stayed that way until June of 1961 when it went down to  $5\frac{1}{2}$  again. It went up to 6 per cent in 1962 and back down to  $5\frac{3}{4}$  in November 1962. Then in December 1965, roughly, it went up to 6 per cent.

These are fluctuations that chartered banks experienced throughout that period of 21 years.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): In the last period, Mr. Paton, which you mentioned, when it goes up to 6 per cent, has this been the period of tight money conditions?

Mr. PATON: Yes, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then is it not safe to assume that in such conditions your interest rates have tended to go right to the ceiling?

Mr. PATON: Yes they have, but there is no alternative where you have a ceiling which is quite artificial, and that is the rates situation now. There is just no possibility that it would be anything else than at the ceiling at the present time.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): With the ceiling removed and with the continuation of tight money conditions which Mr. Coleman said was likely to obtain for some time, what are the forces that will prevent interest rates, including bank interest rates, from continuing to rise? There will be no ceiling for them to press on.

Mr. FULTON: That is not quite accurate because if interest rates rise the prime rate and the government borrowing rate will stay up and as long as that happens there is this ceiling, even though it is a flexible one. I think your question is not based on quite the right premise. Would you not agree that so long as there is tight money you are going to be operating under an interest ceiling, roughly speaking, under the present formula?

Mr. PATON: Based on the interest rates being removed?

Mr. FULTON: Yes.



Mr. PATON: Yes, that would be accurate.

Mr. LAMBERT: Well is there not a tendency for the maximum to become the minimum in a tight money situation.

Mr. COLEMAN: That is what has happened. I think, Mr. Cameron, that competition has to take care of it. When you free the rate then it is entirely up to competition. It is true that in a tight money period you would be competing at higher rates, but competition should take care of it.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I am not wholly convinced that competition should be found on that side of the ledger. The competition, as I see it, should be based on the deposits.

Mr. COLEMAN: I would hope that the information that Mr. Paton gave you with regard to the movements in the prime rate, would indicate that we have not been changing all the traffic would bear.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You have in this period of tight money, you have gone up to the limit. I can only assume that you have gone up to the limit, because you have not, been faced with any problem of competition in placing loans.

Mr. PATON: The loan demand has been such that we have not been able to handle it. On that basis, Mr. Cameron, you are right.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Is this not the very reversal of competitiveness?

Mr. PATON: But do not forget that we are faced with an artificial hindrance in our operation and, therefore, you cannot have anything else but the situation referred to. It should be remembered too that the general level of interest rates is not something that the banks would be able to directly govern; this is a Bank of Canada function. Therefore, they will have the same control over interest rates generally and we will be a part of the competing institutions.

(Translation)

The CHAIRMAN: Have you a question, Mr. Latulippe?

Mr. LATULIPPE: Mr. Chairman, I must conclude that all that is physically possible is not financially possible, is that right? If you have not got the money, if you are short of money, obviously you cannot realize all that you want. What is physically possible is not always financially realizable.

The CHAIRMAN: Would you relate that question to the subject matter of the discussion we are having at present?

Mr. LATULIPPE: Yes, some of what seems to be accepted is the idea of a money shortage. There are ceilings on this and that. Money is in short supply. A lot of things could be done, a lot of things can be physically carried out, but we have not the money for it. Why? Why should we restrict credit, why should we keep interest rates down, what are the reasons for that? I claim it is easier to make money than to do anything else. The financiers say it is your job to make money, then go ahead and make it.

The CHAIRMAN: This question relates, I believe, more to the total money supply than to the matter of interest rates.

Mr. LATULIPPE: It is not a general policy at all. What I say is that what can be achieved physically should be...

The CHAIRMAN: This is a philosophical consideration. I think it is rather difficult for us to say we are philosophers.

Mr. LATULIPPE: I would have another question to put. I have something else to ask.

(English)

Mr. LAMBERT: Carrying on with what Mr. Cameron said—and I hope he can stay until I get this point across—is it not a fact that in a period of tight money, like today, with this ceiling of 6 per cent, if it was not a fact that you are carrying some  $6\frac{1}{4}$  to  $6\frac{3}{4}$  per cent risk people that you could actually do some business at  $5\frac{1}{2}$  or even  $5\frac{1}{4}$  which would give you the spread but still have an average rate of 6 per cent, since tight money dictates that the rate should be around 6 per cent. However, because of the ceiling, you cannot lend at  $6\frac{1}{2}$  to  $6\frac{3}{4}$ , and you are having to lend to everybody at 6 per cent. Is this a reasonable appreciation of the thinking that goes on?

Mr. PATON: At the moment all banks are loaned to the maximum at 6 per cent.

Mr. LAMBERT: Yes, but that is because you are actually carrying some  $6\frac{1}{2}$  per cent people at 6 per cent. To compensate for that half per cent you are being forced to carry a  $5\frac{1}{2}$  per cent person who should really be a prime rate person at 6 per cent.

Mr. FULTON: He just told me they did not average.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I have to go now, Mr. Chairman, but I do hope Mr. Paton will be able to tell someone in the Committee just how he distinguishes between the 6 and the  $6\frac{1}{4}$  per cent risk. That is one of the mysteries I would like to have solved. I asked Mr. MacKinnon 12 years ago how he decided whether I could borrow money at 6 per cent or would have to pay the 12; he never was able to come up with a satisfactory answer.

The CHAIRMAN: Perhaps it would depend on which side the sun was shining. Perhaps there is an element of mystery in banking after all.

Mr. GRÉGOIRE: Mr. Chairman, will we sit tomorrow morning.

(Translation)

The CHAIRMAN: It is not in our timetable.

(English)

I do not think we will. Our next meeting will be Tuesday morning with the usual three sessions.

My list is as follows, although I am not suggesting we are going to complete it this evening; Mr. Laflamme, Mr. Clermont, Mr. Lind and Mr. Grégoire.

Mr. GRÉGOIRE: I have no other questions.

The CHAIRMAN: Perhaps I should accept this supplementary question of Mr. Wahn to begin with.

Mr. WAHN: It is related, Mr. Chairman, to a question asked earlier by Mr. Cameron. Either Mr. Paton or Mr. Coleman said that when the banks went into

the small loans field, they went in at a rate considerably below the then prevailing rate charged by small loan companies. I wonder if the witness would tell the Committee whether they reduced the rate gradually below the customary rates then charged by the small loan companies, and did the small loan companies then follow the bank rate down? Or, for example, if the small loan companies were charging 20 per cent, did the banks go in on the first instance at 12 per cent?

Mr. PATON: The banks went in at a rate which yielded a satisfactory margin, Mr. Wahn, bearing in mind the cost of administering this type of loan. I think I am correct in saying that there is not a very great deal of difference between the rates prevailing today and the original ones, when the banks went into it in 1954. There is some difference but there is not a material difference—and it was not related to any trend in the finance companies' rates.

Mr. WAHN: Since the banks have gone into the small loans field have the small loans companies reduced their rates to compete with the banks?

Mr. PATON: Yes.

Mr. WAHN: Thank you very much.

*(Translation)*

Mr. LATULIPPE: I have another question, Mr. Chairman, if you do not mind. I would like to know how banks answer the requests of the government for loans up to \$25,000 to small industries. I would like to know if banks do lend at 5½%?

Mr. LAVOIE: Yes, Mr. Latulippe, we co-operate with the Government in this field and do make loans of \$25,000. at 5½ per cent.

Mr. LATULIPPE: So the interest rate is at 5½ per cent. I was told lately that banks retained 10 per cent of the amount, is that a fact? Do the banks retain 10 per cent of the loan, \$500. out of the \$5,000.?

Mr. LAVOIE: I do not believe that to be the case.

Mr. LATULIPPE: I was told that was the way it worked.

Mr. LAVOIE: I do not believe that is the case. I do not believe that banks are doing this. That is not the system we are working on.

The CHAIRMAN: Since Mr. Laflamme will be in the chair Tuesday morning, perhaps with one or two minutes remaining I might ask you a very brief question that might be of interest to the committee.

Do the banks consider that balances which are held in deposit accounts—perhaps we should call them current accounts—for commercial customers and on which they do not pay interest, to be, in effect, a form of compensation for the servicing of these accounts in as much as they can loan out that money at the commercial rate of interest without having, in turn, to pay interest to the depositors?

Mr. PATON: These are demand deposits on which we pay no interest and are part of our loanable funds.

The CHAIRMAN: You do not have to pay interest on them. Do you agree with me that in effect it is quite an advantage to the banks to have a sizable amount of funds of that nature available to them? Would you agree that it is a sufficiently



great advantage that in many cases it would justify not charging either a service charge or compensating balances?

Mr. COLEMAN: I think you are talking about compensating balances, are you not? I think you talked about current account balances. I am not so sure about that last question.

The CHAIRMAN: You have a large number of current accounts in which there are various amounts of funds on deposit from time to time. I am not referring to the amount you require to be there.

Mr. COLEMAN: Oh yes, I see, sure.

The CHAIRMAN: If you do not pay interest on these amounts, and you have them as part of your assets to loan at 6 per cent, that is quite an advantage for you.

Mr. COLEMAN: I agree.

The CHAIRMAN: Why could not it be said that the advantages are such that it would justify you not charging either service charges or asking for compensating balances with respect to those accounts?

Mr. COLEMAN: On another account you mean?

The CHAIRMAN: On the same account.

Mr. PATON: That is the situation.

Mr. COLEMAN: Well that is the situation that exists. If the balances carried are sufficient to compensate the bank for the operation of the account, there would be no service charges and those in fact would be the compensating balances?

The interest free deposit and current account in a deposit account would be the compensating balances.

The CHAIRMAN: Well, could not you apply that argument to the whole bundle of money on deposit in current accounts?

Mr. COLEMAN: We do, but we frequently have large amounts of deposits in excess of what we require to compensate us for the work involved. But this is up to the customer who leaves the money with us.

The CHAIRMAN: A large percentage of these deposits belong to the people who do not borrow; they are deposit accounts.

Mr. COLEMAN: Just deposit accounts, you see. Perhaps a good example of this compensating balance which seems hard to clarify, is the amount of \$100,000,000 which the Government of Canada leaves with the banks that gives us some compensation for the work we do for the Government of Canada.

The CHAIRMAN: That is really what led me to ask the question.

Mr. COLEMAN: Is it? You see there are the millions of cheques we process for the Government of Canada, the millions of coupons, the work we do for them, transfers of funds and so on. This is how we get some compensation. They do not pay us a service charge. We get compensation by their leaving with us one hundred million dollars in free balances. Anything over and above that, we pay interest to the government.

The CHAIRMAN: Would you say then that you have no deposit accounts—if I am using the right term—

Mr. COLEMAN: That is a better word to use than current account.

The CHAIRMAN: —which maintain balances of some size on a regular basis, for which you ask neither compensating balances nor service charges?

Mr. COLEMAN: Well, balances in deposit accounts, Mr. Chairman, are compensating balances.

The CHAIRMAN: They would not be unless you asked for a higher balance to be kept there?

Mr. COLEMAN: Well, we would only ask if the activity in the account was such that the bank felt it was losing money on the operation of the account.

Mr. LAMBERT: It is a bad word.

Mr. COLEMAN: Yes, it is a bad word.

The CHAIRMAN: I do not know to what word you are referring.

Mr. LAMBERT: Compensate. A lot of customers want to have printed on their cheques "Negotiable without charge at any branch of this bank or any other chartered bank in Canada". That has a tremendous prestige value to the firm whose cheque it is. Of course, the bank must be reimbursed for handling these cheques, and the whole banking system has exchange charges.

Mr. COLEMAN: Perhaps a better term would be "working balances".

The CHAIRMAN: Would you suggest that?

Mr. COLEMAN: Do you mean should we use "working balances"?

The CHAIRMAN: Or service charges, as an alternative.

Mr. COLEMAN: Working balances are not service charges.

The CHAIRMAN: Gentlemen, I think it is time to adjourn.

## APPENDIX Q

## BANK "A"

## TABLE OF COSTS

for a Personal Instalment Loan or Advance  
in the Principal Amount of \$1,000

Repayable in approximately equal monthly instalments as indicated

	12 months	24 months	36 months
<i>Total loan cost</i> .....	\$ 52.48	\$102.77	\$173.95
<i>Components</i>			
Interest or discount .....	33.13	64.87	99.40
Service or administration charge ....	19.35	37.90	74.55
<i>Other exigible charges* or fees**</i>			
Charge on late payment .....	Yes		
Fee for collecting late payment .....	Yes		
Fee for postponing payment .....	Yes		
Charge for changing payment date .....	Yes		
Fee for life insurance .....	No		
Fee for perfecting security documents .....	No		

## BANK "B"

## TABLE OF COSTS

for a Personal Instalment Loan or Advance  
in the Principal Amount of \$1,000

Repayable in approximately equal monthly instalments as indicated

	12 months	24 months	36 months
<i>Total loan cost</i> .....	\$ 60.00	\$116.00	\$168.00
<i>Components</i>			
Interest or discount .....	32.50	62.50	92.50
Service or administration charge ....	27.50	53.50	75.50
<i>Other exigible charges* or fees**</i>			
Charge on late payment .....	Yes		
Fee for collecting late payment .....	No		
Fee for postponing payment .....	Yes		
Charge for changing payment date .....	No		
Fee for life insurance .....	No		
Fee for perfecting security documents .....	No		

\* Charges are usually on a percentage basis.

\*\* Fees are usually on a prescribed dollar basis.



## BANK "C"

## TABLE OF COSTS

for a Personal Instalment Loan or Advance  
in the Principal Amount of \$1,000

Repayable in approximately equal monthly instalments as indicated

	12 months	24 months	36 months
Total loan cost .....	\$ 54.86	\$108.04	\$162.07

*Components*

Interest or discount .....	31.96	61.98	92.60
Service or administration charge ....	22.90	46.06	69.47

*Other exigible charges\* or fees\*\**

Charge on late payment .....	Yes
Fee for collecting late payment .....	No
Fee for postponing payment .....	No
Charge for changing payment date .....	No
Fee for life insurance .....	No
Fee for perfecting security documents .....	No

## BANK "D"

## TABLE OF COSTS

for a Personal Instalment Loan or Advance  
in the Principal Amount of \$1,000

Repayable in approximately equal monthly instalments as indicated

	12 months	24 months	36 months
Total loan cost .....	\$ 53.96	\$108.08	\$162.08

*Components*

Interest or discount .....	32.50	62.50	92.50
Service or administration charge ...	21.46	45.58	69.58

*Other exigible charges\* or fees\*\**

Charge on late payment .....	Yes
Fee for collecting late payment .....	Yes
Fee for postponing payment .....	Yes
Charge for changing payment date .....	Yes
Fee for life insurance .....	No
Fee for perfecting security documents .....	No

\* Charges are usually on a percentage basis.

\*\* Fees are usually on a prescribed dollar basis.

## BANK "E"

## TABLE OF COSTS

for a Personal Instalment Loan or Advance  
in the Principal Amount of \$1,000

Repayable in approximately equal monthly instalments as indicated

	12 months	24 months	36 months
<i>Total loan cost</i> .....	\$ 53.13	\$109.59	\$174.85
<i>Components</i>			
Interest or discount .....	53.13	109.59	174.85
Service or administration charge ....	—	—	—
<i>Other exigible charges* or fees**</i>			
Charge on late payment .....		Yes	
Fee for collecting late payment .....		No	
Fee for postponing payment .....		Yes	
Charge for changing payment date .....		Yes	
Fee for life insurance .....		No	
Fee for perfecting security documents .....		Yes	

## BANK "F"

## TABLE OF COSTS

for a Personal Instalment Loan or Advance  
in the Principal Amount of \$1,000

Repayable in approximately equal monthly instalments as indicated

	12 months	24 months	36 months
<i>Total loan cost</i> .....	\$56.50	\$110.50	\$164.50
<i>Components</i>			
Interest or discount .....	32.50	62.50	92.50
Service or administration charge ....	24.00	48.00	72.00
<i>Other exigible charges* or fees**</i>			
Charge on late payment .....		Yes	
Fee for collecting late payment .....		Yes	
Fee for postponing payment .....		Yes	
Charge for changing payment date .....		Yes	
Fee for life insurance .....		No	
Fee for perfecting security documents .....		No	

\* Charges are usually on a percentage basis.

\*\* Fees are usually on a prescribed dollar basis.

## BANK "G"

## TABLE OF COSTS

for a Personal Instalment Loan or Advance  
in the Principal Amount of \$1,000

Repayable in approximately equal monthly instalments as indicated

	12 months	24 months	36 months
<i>Total loan cost</i> .....	\$ 52.12	\$101.18	\$168.32
<i>Components</i>			
Interest or discount .....	33.12	64.78	98.92
Service or administration charge ....	19.00	36.40	69.40
<i>Other exigible charges* or fees**</i>			
Charge on late payment .....		Yes	
Fee for collecting late payment .....		No	
Fee for postponing payment .....		Yes	
Charge for changing payment date .....		No	
Fee for life insurance .....		No	
Fee for perfecting security documents .....		No	

## BANK "H"

## TABLE OF COSTS

for a Personal Instalment Loan or Advance  
in the Principal Amount of \$1,000

Repayable in approximately equal monthly instalments as indicated

	12 months	24 months	36 months
<i>Total loan cost</i> .....	\$ 52.96	\$103.98	\$155.60
<i>Components</i>			
Interest or discount .....	31.96	61.98	92.60
Service or administration charge ....	21.00	42.00	63.00
<i>Other exigible charges* or fees**</i>			
Charge on late payment .....		Yes	
Fee for collecting late payment .....		Yes	
Fee for postponing payment .....		Yes	
Charge for changing payment date .....		No	
Fee for life insurance .....		No	
Fee for perfecting security documents .....		No	

\* Charges are usually on a percentage basis.

\*\* Fees are usually on a prescribed dollar basis.



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OF  
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LÉON-J. RAYMOND,  
*The Clerk of the House.*

HOUSE OF COMMONS  
First Session—Twenty-seventh Parliament  
1966

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STANDING COMMITTEE  
ON  
**FINANCE, TRADE AND ECONOMIC AFFAIRS**

*Chairman:* Mr. HERB GRAY

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MINUTES OF PROCEEDINGS AND EVIDENCE  
No. 25

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TUESDAY, NOVEMBER 22, 1966

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Respecting  
Bill C-190, An Act to amend the Bank of Canada Act.  
Bill C-222, An Act respecting Banks and Banking.  
Bill C-223, An Act respecting Savings Banks in the Province of Quebec.

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WITNESSES

*From The Canadian Bankers' Association:* Messrs. S. T. Paton, President;  
Leo Lavoie, Vice-President; J. H. Coleman, Vice-President; R. M.  
MacIntosh, Joint General Manager, Bank of Nova Scotia; W. J.  
Dixon, Deputy General Manager, Bank of Nova Scotia.  
*And also:* C. F. Elderkin, Inspector General of Banks.

ROGER DUHAMEL, F.R.S.C.  
QUEEN'S PRINTER AND CONTROLLER OF STATIONERY  
OTTAWA, 1966

STANDING COMMITTEE  
ON  
FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. Herb Gray

*Vice-Chairman:* Mr. Ovide Laflamme

and Messrs.

Addison,	Comtois,	Latulippe,
Basford,	Flemming,	Lind,
Cameron ( <i>Nanaimo-</i>	Fulton,	McLean ( <i>Charlotte</i> ),
<i>Cowichan-The Islands</i> ),	Gilbert,	Monteith,
Cashin,	Irvine,	More ( <i>Regina City</i> ),
Chrétien,	Johnston,	Munro,
Clermont,	Lambert,	Valade,
Coates,	Lamontagne,	Wahn—(25).

Dorothy F. Ballantine,  
*Clerk of the Committee.*



## REPORT TO THE HOUSE

WEDNESDAY, November 23, 1966.

The Standing Committee on Finance, Trade and Economic Affairs has the honour to present its

### SIXTEENTH REPORT

Your Committee notes that the authority to carry on the business of banking by the chartered banks under the Bank Act and by the savings banks under the Quebec Savings Banks Act will expire on the first day of December, 1966, unless extended by Parliament.

Your Committee is of the opinion that it is not possible to complete its examination of the two bills to revise these Acts, namely Bills C-222 and C-223, before that date and respectfully requests that Parliament extend the authority under the present Acts for a period of four months to the first day of April, 1967, or such later date as it may consider appropriate.

Respectfully submitted,

HERB GRAY,  
*Chairman.*



## MINUTES OF PROCEEDINGS

TUESDAY, November 22, 1966.

(46)

The Standing Committee on Finance, Trade and Economic Affairs met at 11.15 a.m. this day, the Vice-Chairman, Mr. Laflamme, presiding.

*Members present:* Messrs. Addison, Cameron (*Nanaimo-Cowichan-The Islands*), Clermont, Comtois, Flemming, Fulton, Gilbert, Johnston, Laflamme, Lambert, Latulippe, Lind, More (*Regina City*)—(13).

*Also present:* Messrs. Grégoire and Thompson.

*In attendance:* Messrs. S. T. Paton, President, The Canadian Bankers' Association and Vice-President and Chief General Manager, The Toronto-Dominion Bank; Leo Lavoie, Vice-President, The Canadian Bankers' Association and Vice-President and General Manager, La Banque Provinciale du Canada; J. H. Coleman, Vice-President, the Canadian Bankers' Association and Chief General Manager, The Royal Bank of Canada; W. T. G. Hackett, General Manager (Investments), Bank of Montreal and Chairman of Canadian Bankers' Association Bank Act Revision Committee; Gilles Mercure, Assistant General Manager, La Banque Provinciale du Canada; F. L. Rogers, Economic Adviser, The Bank of Nova Scotia and Chairman, Canadian Bankers' Association Economists Committee; W. J. Dixon, Deputy General Manager, Bank of Nova Scotia; R. M. MacIntosh, Joint General Manager, Bank of Nova Scotia; J. H. Perry, Executive Director, The Canadian Bankers' Association; C. F. Elderkin, Inspector General of Banks; Miss M. R. Prentis, research assistant.

The Committee resumed consideration of the banking legislation.

On motion of Mr. Lambert, seconded by Mr. Cameron (*Nanaimo-Cowichan-The Islands*),

*Resolved,*—That the Committee report to the House as follows:

Your Committee notes that the authority to carry on the business of banking by the chartered banks under the Bank Act and by the savings banks under the Quebec Savings Banks Act will expire on the first day of December, 1966, unless extended by Parliament.

Your Committee is of the opinion that it is not possible to complete its examination of the two bills to revise these Acts, namely Bills C-222 and C-223, before that date and respectfully requests that Parliament extend the authority under the present Acts for a period of four months to the first day of April, 1967, or such later date as it may consider appropriate.

Questioning of the witnesses was resumed and Messrs. Paton, Lavoie, MacIntosh, Coleman and Elderkin were questioned.

At 12.55 p.m., the Committee adjourned until 3.45 p.m. this day.



## AFTERNOON SITTING

(47)

The Committee resumed at 3.45 p.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Addison, Cameron (*Nanaimo-Cowichan-The Islands*), Chrétien, Clermont, Comtois, Flemming, Fulton, Gilbert, Gray, Johnston, Laflamme, Lambert, Latulippe, Lind—(14).

*Also present:* Messrs. Grégoire and Thompson.

*In attendance:* The same as at the morning sitting.

Messrs. Paton, MacIntosh, Dixon and Elderkin answered questions put to them by the Committee.

Mr. Paton tabled forms requested at the meeting of November 17, 1966, namely, samples of forms used by the chartered banks involving a charge to the customer, and the Clerk was directed to distribute copies to the members.

At 5.55 p.m. the Committee adjourned until 9.00 p.m. this day.

## EVENING SITTING

(48)

The Committee resumed at 9.05 p.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Cameron (*Nanaimo-Cowichan-The Islands*), Chrétien, Clermont, Comtois, Fulton, Gilbert, Gray, Johnston, Laflamme, Lambert, Latulippe, Lind, Munro, Wahn—(14).

*Also present:* Messrs. Caouette, Grégoire and Thompson.

*In attendance:* The same as at the morning sitting and Mr. Denis Baribeau, research assistant.

Questioning of the witnesses was continued, and at 10.20 p.m. the Committee adjourned until Thursday, November 24, 1966, at 11.10 a.m.

Dorothy F. Ballantine,  
Clerk of the Committee.

## EVIDENCE

(Recorded by Electronic Apparatus)

TUESDAY, November 22, 1966.

The VICE-CHAIRMAN: Gentlemen, now that I see a quorum I will ask for a motion. As everyone knows, the consensus is that there is no possibility of getting through the hearing and study of the briefs before the end of November. At the end of November, the Bank Act and the Quebec Savings Banks Act will expire. Accordingly, I have been asked, with the concurrence of the members of the Committee, to report to Parliament so that the Minister of Finance can ask Parliament to agree to an extension of the effect of these acts.

May I have a mover and seconder for the following motion:

Your Committee notes that the authority to carry on the business of banking by the chartered banks under the Bank Act and by the savings banks under the Quebec Savings Banks Act will expire on the first day of December, 1966, unless extended by parliament.

Your Committee is of the opinion that it is not possible to complete its examination of the two bills to revise these Acts, namely bills No. C-222 and No. C-223, before that date and respectfully requests that Parliament extend the authority under the present Acts for a period of one month to the first day of January, 1967, or such later date as it may consider appropriate.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I would suggest, Mr. Chairman, that we should not limit the extension to one month. My suggestion would be to make it at least three months. We may be through before that time, and if so that will be all right.

The Vice-Chairman: If we do pass this motion it will give authority for the law to be effective up to perhaps, the middle of April, because—

Mr. ELDERKIN: May I explain?

The VICE-CHAIRMAN: Yes, please, Mr. Elderkin.

Mr. ELDERKIN: The present extension in the bill is the 1st of January, or a date of that kind, but it also says, as in the present act, that if Parliament does not sit for 20 days during the final month—which, in this case, would be during December—then the powers are extended for 60 sitting days thereafter. Now, the bill reads, “the 1st of January, 1967,” but it is obvious that Parliament will not sit for 20 sitting days in December; there are only 17 sitting days before Christmas in December. The result is that there will be an automatic extension, possibly up to the middle of April, because Easter comes in March.

Mr. LAMBERT: Mr. Chairman, notwithstanding the observations made by Mr. Elderkin, it is my view, in the light of what the Minister told me in reply to a question the other day, that the bill would be introduced last week for this

extension. I realize, as Mr. Elderkin has pointed out, that under section 6 of the present act there is an automatic 60 sitting days' extension, but there is no guarantee that, because of unforeseen circumstances, Parliament might not have to sit between the December 25th and January 31st. If we go right to Christmas Eve, shall we say, or a couple of days before that, and get our 17 days in, we would have only 3 days, in which there would be a horrible scramble.

My view is that since there is a great deal of work to be done in Committee hearing the briefs, in clause-by-clause study, in the House, and then over in the Senate, the date of April 1st would be the most satisfactory date for an extension, to give us the proper latitude. I am not at all concerned about an extra month if we are going to do a proper job.

My view, Mr. Chairman, is that the recommendation to the House from this Committee should be that the act be extended to April 1st. You might want to include with that "or such earlier date, in the event that parliament shall have approved a new bank act".

Mr. ELDERKIN: You would not need that. The new bank act would override it.

Mr. LAMBERT: All right; that is fine. But I would not like us to come again, undignified, to parliament, and before everybody, say that we have not completed our work.

The VICE-CHAIRMAN: In that case we could have this motion amended. Instead of saying "for a period of one month to the first day of January, 1967", it can be changed to "for a period of four months to the first day of April, 1967." Is this motion agreeable to the members?

Mr. LAMBERT: I so move.

Mr. CAMERON: I second the motion.

Motion, as amended, carried.

The VICE-CHAIRMAN: The Chairman has not given to me the list of the members who wanted to ask questions and I would ask the members to indicate to me—Mr. Flemming, please. We are still on the interest rates, I understand.

Mr. FLEMMING: Mr. Chairman, I am going to ask a little indulgence. There are a few questions which I have not had an opportunity to ask, and if I wander a bit, Mr. Chairman, I hope you will forgive me.

I would like to ask Mr. Paton if he is satisfied, from the examination that he and his associates have made of the new bill which is before us, that it recognizes the fact that the country in the next ten years will make, we hope, the same degree of, or perhaps even more, progress commercially than it has in the last ten, and whether the bill in his opinion, makes the changes necessary to meet the increased tempo which I think this country will have.

Mr. PATON (*President, The Canadian Bankers' Association*): Bearing in mind, Mr. Flemming, that we are on the question of interest rates?

Mr. FLEMMING: Yes, I did not read it very well.

Mr. PATON: I would say—and this confirms, I think, what we suggested last week—that there is not enough flexibility in the suggested two-phase removal of the interest rate ceiling.



The Bankers' Association strongly reiterate their position that, in view of the potential economic development during the forthcoming decade, the interest rate ceiling should be removed entirely as of this revision.

Mr. FLEMMING: And you think the change in the interest rate and the enlargement of the scope of your activities so far as mortgage lending and so on are concerned will increase your ability to make what is generally known as "term loans". Do you think that the making of term loans, even though you felt obliged to charge more interest—which I am sure would be greatly against your natural inclinations—would bring about a more than ordinary development of business in the country?

Mr. PATON: I agree, Mr. Flemming. The technical changes in the act, permitting us to get into other forms of lending, would enable us to participate in the development of Canada to a much greater degree over the next ten years. I would think, that with the one reservation I have already expressed, regarding interest rates, the powers given to us under this bill would be essentially satisfactory to the banks.

Mr. FLEMMING: Do you think that the increase or the elimination, if you like, of the ceiling on interest rates would enable quite a large class of borrowers to borrow at a more advantageous rate, from their point of view, than at present?

Mr. PATON: That is correct; that is our feeling.

Mr. FLEMMING: I am sure that most of your members do have a degree of lending on time limit and terms, and that in that connection you undoubtedly find yourself exposed to a good deal of competition and knowledge of competition. I presume that is the basis on which you agree that this would be an improvement in the rate paid by ordinary, smaller borrowers?

Mr. PATON: That is correct. The area of competition would be enlarged with our entry into it, and would benefit the borrower, particularly the smaller one.

Mr. FLEMMING: Since we have dealt with the matter of term loans, I believe that any other questions that I would have asked have been put by my fellow members of the Committee, so I think that is all, Mr. Chairman. Thank you very much.

The VICE-CHAIRMAN: I will call on Mr. Clermont.

Mr. LIND: I was going to ask about RoyNat while we had Mr. Coleman in the chair as a witness, but I understand that we are not supposed to discuss RoyNat yet, or are we?

The VICE-CHAIRMAN: No; I brought your attention to the fact that you are not supposed to go outside the Royal Bank brief.

Mr. LIND: Perhaps I could pass for a few minutes until I get this ironed out.

The VICE-CHAIRMAN: Before you begin, Mr. Clermont, may I interject to say, with respect to the question asked by Mr. Lind, that a report on RoyNat has been included in the brief presented by the Royal Bank, so that when this brief is before us I think you might have an opportunity of asking questions regarding this report.

(Translation)

Mr. CLERMONT: I would have a question to put to Mr. Lavoie. The chartered banks make short-term loans to the Federal Government, if so, at what interest rate?

Mr. LAVOIE: To the Federal Government? No, I do not think so. You mean a direct loan?

Mr. CLERMONT: No, not a direct loan. The interest on deposits are paid on a 3 month basis minimum.

Mr. LAVOIE: Yes.

Mr. CLERMONT: Does this mean that if the depositor has a balance of \$5,000 in his savings account for an 11-month period—and we will stick to that period, and withdraws \$4,900 in the last week. Does this mean that the interest will be paid only on \$100?

Mr. LAVOIE: The interest is based on the minimum three month balance. If, for instance, a customer has a \$5,000 deposit over 90 days, then we will pay an interest of 3 percent on the balance of that \$5,000. However, if there is a withdrawal during that 3-month period, and if the amount is lowered to \$900 or to \$100 for instance, he would be paid the interest on the latter balance at 3 percent.

Mr. CLERMONT: This means that he will not be able to have interest on the balance of the amount over that 3-month period?

Mr. LAVOIE: Not on ordinary savings accounts which are chequing accounts.

Mr. CLERMONT: Supposing your depositor makes a loan. Does he wait three months before making his withdrawal?

Mr. LAVOIE: This has happened, Mr. Clermont.

Mr. CLERMONT: With regard to the removal of the interest ceiling, it has been claimed that by removing that interest rate ceiling, this would allow banks to pay higher dividends to shareholders. Are you limited to any percentage of dividends to your shareholders at the present time?

Mr. LAVOIE: Mr. Clermont, I do not believe the removal of the interest rates would automatically allow for an increase in the dividend. It might increase the interest rates paid to depositors, but with regard to dividends, I would like to say this. Actually, dividends are paid on profits after taxes. This dividend is declared according to the income of the bank over a year.

Mr. CLERMONT: But are you limited to a certain percentage of dividends?

Mr. LAVOIE: There is no such limitation as regards dividends we can pay. At least I do not think so.

Mr. CLERMONT: What about 6 and 70? Clause 70, sub-clause 3?

Mr. LAVOIE: In sub-clause 3 of clause 71, it is stated that no division of profits exceeding the rate of 8 per cent per annum on the paid-up capital stock of the bank shall be made by the bank unless after making the division, the bank has a rest account equal to at least 30 per cent, etc.

Mr. CLERMONT: We have been told that we should remove the interest rates, which would allow you to recover deposits which are made at present in the near

banks who are not limited to an interest rate of 6 per cent. However, if I refer to a question put by the Member for Charlotte to Mr. Coyne as appears in our Minutes, No. 1, Mr. Coyne answered: "about the mortgage companies increasing the business under the six per cent ceiling in competition with the banks, I would say that if they were subject to the same ceiling as the banks and if they did not have the advantages the banks have, I do not think they could have competed successfully. But the banks have so many advantages over mortgage and finance companies that the advantage lies with them." Do you accept that statement? Do you think that the banks do enjoy advantages over other financial institutions or mortgage companies?

Mr. LAVOIE: Well, it depends. You know that banks have advantages, but they also have disadvantages. We should not forget that chartered banks have to maintain with the Bank of Canada an 8 per cent reserve which is an unproductive asset, that is, an interest-free asset. Then they have a secondary reserve of 7 per cent at the same time, which is limited to investments in Treasury bonds. This puts the chartered banks under some disability. With regard to the interest rate, I am convinced, Sir, that if the interest ceiling were removed, quite probably banks would be able to pay better interest rates on savings, could increase their deposits and in consequence, would be in a position to make far more smaller loans to small borrowers. You know that small borrowers want to deal with banks, and that is about the only source they have of cheap loans. If banks would be able to lend more to small manufacturers, merchants, etc., I am convinced that...

Mr. CLERMONT: What do you mean by cheap money? If the ceiling rate were completely removed, what would happen?

Mr. LAVOIE: It is rather difficult to answer that question. It is understood that under the terms of the new Act there would not be any agreement on banks in respect of the interest rates on deposits and the interest rate on loans. In the absence of an agreement, there will be no possibility of discussing this between bankers. This will be entirely prohibited. If, for instance, in a community, one bank meets competition through two other branches, I am convinced that the bank manager will bestir himself to discover what his competitor is charging by way of interest rate on loans. I am convinced that he will have to meet that competition. This would be a matter of supply and demand, of competition.

Mr. CLERMONT: But I believe that in the public's mind, there is a feeling abroad at certain times that there is no competition.

Mr. LAVOIE: But there is competition. There always has been.

Mr. CLERMONT: As far as the number of branches is concerned.

Mr. LAVOIE: But there always has been competition between the banks themselves. If the customer is not satisfied with the services he obtains from one bank, he can go to another and might obtain more advantageous rates from the latter.

Mr. CLERMONT: According to the statistics we have at the present time, there are more branch banks in Canada per capita than in the United States. I believe in the United States we have one branch for 5,500 people, whereas the figure for Canada is 3,500. Do you have that information?



Mr. LAVOIE: Yes, I have that information in respect of the number of chartered banks in Canada. In 1965, we had 5,724 branches in Canada. For foreign countries, the United States more particularly, I do not have that information.

Mr. CLERMONT: I believe it is a little more than 14,000.

Mr. LAVOIE: I do not have that information, Sir.

Mr. CLERMONT: In any event, Mr. Chairman, I believe that the figure for the United States is a little over 14,000. Is the Association of Chartered Banks satisfied that competition does exist?

Mr. LAVOIE: Yes, there is undoubtedly competition between the banks.

Mr. CLERMONT: There is no form of agreement between the banks with regard to customers who attempt to open an account in any of the branches?

Mr. LAVOIE: I do not think such agreements can exist. They certainly could not be applied. If you have two or three branches of a bank in one place, the managers would be out looking for business. And even if there were an agreement, the manager would not be inclined to accept. What the Branch manager always anxious to obtain more customers, even at the expense of another bank.

The VICE-CHAIRMAN: Have you finished, Mr. Clermont?

*(English)*

Now I will recognize Mr. Lind. Mr. Lind, you did indicate to me at the opening of the session that you would like to ask some questions.

Mr. LIND: The only thing that I would like to add, Mr. Chairman, is to ask if there are any data available on the losses on bad debts incurred by the chartered banks?

Is there a separate sheet that shows us what their losses by year are through write-offs of bad debts?

Mr. PATON: Mr. Elderkin, in his evidence, supplied statistics regarding the reserves total and the total reserves permissible. The indication was that the actual reserves were 75 per cent of par. The latter if I recall correctly, comes to some four hundred and—

Mr. LIND: I am not interested so much in the reserves as I am in the amount written off.

Mr. PATON: No, this is not available. This is a matter for each individual bank, and they are not collated in any way.

Mr. LIND: There is no way of telling to what extent it might happen over the pool by your association of the eight chartered banks?

Mr. PATON: I gave some figures last week on our loss experience, percentage wise, if you recall, in relation to risk assets, but that was merely on a percentage basis.

There is a table, Mr. Lind, which we have attached here. I am not too sure from what it is extracted, but it refers to additions to shareholders' equity and inner reserves for 25-year periods. Has that been tabled, Mr. Elderkin?

Mr. ELDERKIN: Yes.

Mr. PATON: Mr. Elderkin tells me that it has been tabled; that the Committee has it. It is taken from the Bank of Canada's statistical summary, and will be found at page 12.

Mr. LIND: This does not give us any breakdown with regard to actual write-offs, does it?

Mr. PATON: No; this refers to totals and loss-experience expressed in a percentage.

Mr. LIND: You have no tables that would give us this breakdown?

Mr. PATON: No, sir.

Mr. LIND: Is there any reason why we should not have this information?

Mr. PATON: I think so; I think there is very good reason. This gets to the very core of a bank's operations. These operations are thoroughly vetted and thoroughly audited by Mr. Elderkin, and, through him, by the minister. The minister, of course, is fully aware of the entire position of each and every bank. It would not appear to me to be in the interest of the public, nor in the interest of the banks, to publish these figures.

Mr. LIND: If these figures were available, would the banks worry or be concerned about competition finding out their losses? Or would it be in the public interest to know what these losses are?

Mr. PATON: I think, perhaps, we are getting into another item in the brief regarding disclosure or nondisclosure. Certainly no bank, that I know of, is concerned about another bank having knowledge of its particular operation; I think we all have adequate confidence in our own operations and would feel quite satisfied to compare one against the other.

Is that the import of the question?

Mr. LIND: We find these financial institutions such as Prudential or Atlantic Finance getting into trouble. I was wondering if we had any comparison of the loss incurred by the chartered banks; they must, in some years have had very substantial losses.

The VICE-CHAIRMAN: I do not want to interrupt your questioning, but I must remind hon. members that we had already decided to relate our questioning, as much as possible, to interest rates. I think we are going a little further now.

Mr. LIND: I will concede that I am off interest rates, Mr. Chairman.

The VICE-CHAIRMAN: Yes. Do you have any other questions on interest rates?

Mr. LIND: When will we have a chance of getting off interest rates? This has been discussed now for two or three days.

The VICE-CHAIRMAN: As soon as we finish our questioning.

Now I will recognize Mr. Grégoire.

*(Translation)*

Mr. GRÉGOIRE: What I would like to know is this. Because the complete removal of the interest ceiling will take place when the yield of short-term government bonds will fall under  $4\frac{1}{4}$  per cent for 3 months, I would like to know when the yield on the short-term bonds was  $4\frac{1}{2}$  per cent?

(English)

Mr. ELDERKIN: May I give you that answer this afternoon, Mr. Grégoire?

Mr. GRÉGOIRE: All right.

An hon. MEMBER: That has been tabled.

Mr. GRÉGOIRE: When?

Mr. ELDERKIN: I do not have it with me; that is the unfortunate part of it.

Mr. MACINTOSH: I have that information.

The VICE-CHAIRMAN: Mr. MacIntosh has this information and can provide it for us.

Mr. MACINTOSH: Mr. Grégoire, I have before me a press release of the Minister of Finance, issued in July of this year, at the time that this procedure was announced, that there would be provided in the Bank Act the so-called trigger clause—that is, the clause for removal of the 6 per cent ceiling altogether. Those statistics show the three month moving average of yields on Government of Canada bonds due within three years, monthly from 1956 through July 1966, and the August figures have been added to the table.

The level of interest rates was last below  $4\frac{1}{2}$  per cent in August 1965. I might add that the number of occasions on which the average rate has been in excess of  $4\frac{1}{2}$  per cent for any extended period, has been, roughly speaking, three or four times within the last 10 years; there have been cyclical periods when Government of Canada interest rates have gone above that level. In recent years they have gone higher and stayed up longer than before, and under the same conditions of economic growth that we have now no change is really in sight; and if you will note press reports on the day of the annual report of the Economic Council of Canada, there is no real indication that, under present conditions, the level of rates will drop.

(Translation)

Mr. GRÉGOIRE: Mr. Chairman, what I would like to know is this. Because you do not foresee that the average yield will fall in any near future to  $4\frac{1}{2}$  %, is it to the advantage of the banks for the average yield to be as high as possible, so that by adding  $1\frac{3}{4}$  per cent your interest rate will be as high as possible.

(English)

Mr. MACINTOSH: Mr. Grégoire, there is no clear evidence on whether financial institutions are better off, in terms of their own position, with high interest rates or low interest rates. There have been some extensive studies of this subject in the United States, with no conclusive result.

A financial institution is interested in the margin between the cost of its funds, and the rate of return on its funds. If interest rates are high it does not necessarily follow that banks are, for that reason, better off in terms of their margin of profit; it may simply mean that they are able to pay a higher rate to depositors. And, of course, this is one of our main points, that with freedom from the ceiling we might eventually be able to earn a higher level of interest rate under these conditions, but we would also pay a higher rate. I cannot tell you whether or not our margin would be better or not. This would also depend on other factors such as our costs and expenses and the sufficiency of operations.



(Translation)

Mr. GRÉGOIRE: The higher your interest rate, the higher an interest you can pay to your depositors, is that not a fact? So, to charge a higher interest rate would be to the advantage of the chartered banks. That is a question I put to you a while ago. It would be to the advantage of the chartered banks to have as high a yield on bonds as possible, so that by adding 1 3/4 % to that it will be possible for you to charge as high an interest rate to your borrowers as possible up to a certain limit. It is to the advantage of the chartered banks for the average yield of Government bonds to be higher than it is at the present time so that you may require a higher rate of interest from your borrowers?

(English)

Mr. MACINTOSH: No, sir. You will remember the other evening, when we were discussing this matter, that you were arguing that it would be to our advantage to have a low rate of interest for a few months, and I attempted to argue the proposition that it would be impossible for us to force the market so as to reach a low level of rates.

You are now asking me if it is not to our interest to have a high level of rates, and my answer is that this is not necessarily the case. There is no necessary relationship between the level of our yields on government of Canada bonds at any one moment of time and the level of commercial loan rates, because in the case of any institution which has an investment portfolio, this has been acquired over a very considerable period of time. The fact is that the yields on bond portfolios of banks are certainly not presently on their books at the level of yield on government of Canada bonds today. Perhaps to clarify that I might say that bonds that have been acquired the banks over, shall we say, the last 10 years have been gradually rolled over and rolled over and let us say that the average yield of a bank investment portfolio today might be 4½ per cent; in the current yields they are about 5½ per cent to 5.9 per cent. But there is no close relationship between yields on loans today and yield on bond portfolios which have been built in over many years.

(Translation)

Mr. GRÉGOIRE: These are very long answers to questions I did not actually put. That is why I find it a little complicated. I would like to put this question, the other day I asked whether it was to the advantage of the banks to lower the average yield of these bonds to 4½ per cent so that the limitation on interest rates would completely disappear, and you answered, No. Today I ask you if it is to the advantage of the banks to increase the average yield so that adding 1 3/4 per cent to this figure, will provide more freedom for you in the establishment of the interest rates to borrowers, you answer again, No. You are not interested in having complete freedom as far as interest rates are concerned. At the present time the Bill indicates a practical maximum of 7 per cent because four and a half months ago it was set at 7 per cent. Your are not interested at all in going beyond that figure?

(English)

Mr. MACINTOSH: No, sir; we are interested in removal of the ceiling. In fact I believe Mr. Paton has stated on several occasions at Committee meetings

that it is the view of the banks that we would prefer to see the ceiling removed altogether. Under present conditions—

(Translation)

The CHAIRMAN: The questions you are putting are very complicated and they cannot be answered by yes or no.

(English)

The VICE-CHAIRMAN: Go ahead, Mr. MacIntosh.

Mr. MACINTOSH: Thank you, Mr. Chairman.

I was saying that Mr. Paton has said on several occasions that the banks hold the view that it would be better to remove the ceiling altogether, especially in the light of the economic conditions which have existed since the bill was originally presented to parliament. He has emphasized that we think that we should be free of this restriction which does not apply to other institutions. Naturally, I agree with that view completely.

We also say that under current conditions there does not seem much likelihood that the trigger clause in the Bank Act will lead to the complete removal of the ceiling within the foreseeable future, and we will, therefore, be living with a squeeze on interest rates for some time to come. There is no  $1\frac{3}{4}$  per cent addition to the yield on government bonds after this ceiling has gone. There will be no upward limit on the ceiling on interest rates at that time. The only operative relevance of the level of government of Canada bond yield now is that it affects this transitional period of the ceiling and also affects the time at which the ceiling will go off altogether.

(Translation)

Mr. GRÉGOIRE: Mr. McIntosh, you have just told me, if I understand properly, that you prefer a complete removal of the interest rate ceiling: nor do you favour any transition period of  $1\frac{3}{4}$  per cent. You would prefer then that there would be no ceiling whatever, is that correct? You prefer to be perfectly free as far as interest rates are concerned?

(English)

Mr. MACINTOSH: That is correct.

(Translation)

Mr. GRÉGOIRE: We have an Act called Bill C-222, which indicates that when the average yield of Government bonds will be down to  $4\frac{1}{2}$  per cent there will be complete freedom of interest rates, is that a fact?

(English)

Mr. MACINTOSH: When it has occurred for three month periods.

(Translation)

Mr. GRÉGOIRE: Now since you want complete freedom to charge interest as you please, but since there is an Act and if it is not changed there will have to be this lowering to the  $4\frac{1}{2}$  per cent level for the interest rate to be removed, such being the case, would it not be to the advantage of the chartered banks to see to it that the average yield of Government bonds be  $4\frac{1}{2}$  per cent for a period of 3 months?

(English)

Mr. MACINTOSH: Mr. Chairman, as a free gift to the Minister of Finance I have a suggestion to make in this connection which you might pass on to him. I did not mention it the other evening. It is this: If the banks set out to force down the yield on government of Canada bonds from  $5\frac{1}{2}$  per cent to  $4\frac{1}{2}$  per cent he would have a very attractive market into which to sell a great many government of Canada bonds; and if I were he—and, as I say, I offer this free advice to him—he should sell several billions of government of Canada bonds; as many as we wanted to buy he could sell, and he could go on selling more and more bonds, and then he could use the proceeds to retire the rest of the government of Canada debt, and he therefore would have lowered the cost of the government of Canada debt from the present level of  $5\frac{1}{2}$  to  $4\frac{1}{2}$ , and it would be a splendid proposition for him but a very bad one for us.

(Translation)

Mr. GRÉGOIRE: Now, Mr. Chairman, I want to return to the question I had put before Mr. MacIntosh takes it to the Minister of Finance and through him to the Government. Be that as it may, since the chartered banks want the complete removal of the ceiling, because also we have this provision in the Act stating that when the average yield of short term Government bonds will have been lowered to  $4\frac{1}{2}$  per cent, the chartered banks will then be able to charge the interest rate as they please. This being the case, is it not to the advantage of the chartered banks for this average yield of short term bonds to reach a figure lower than  $4\frac{1}{2}$  per cent as quickly as possible?

(English)

Mr. MACINTOSH: I am not sure that I understand the nature of your question but it is our view that we would like to see the ceiling removed as soon as possible, yes. If interest rates were to fall, with the result that lending rates fell generally, then, of course, so would borrowing rates, and the whole level of interest rates would shift down and we would still face the perennial problem of trying to maintain our margin with the best possible spread. But whether interest rates are generally high or generally low does not indicate what bank profit margins are. We want to see the ceiling removed, of course, and whether or not it is removed at an early date or not will depend on the level of market interest rates which we simply cannot control.

Mr. GRÉGOIRE: You would like to see the ceiling removed?

Mr. MACINTOSH: Yes.

Mr. GRÉGOIRE: And you know that according to the law it can be removed only when the interest rate reaches  $4\frac{1}{2}$  per cent, according to the act. You know that?

Mr. MACINTOSH: That is correct; but we also say that we would like to see the provision for a transitional period taken out altogether. We would simply like to see removal of the ceiling now, on the grounds that monetary conditions have stiffened and tightened very considerably since the bill was first drafted, and we now consider that the  $4\frac{1}{2}$  per cent figure clause is too low a rate in terms of market conditions.

We have also suggested at this committee meeting—I believe Mr. Paton has suggested it on several occasions—that it would be preferable if the trigger rate were raised to 5 per cent, or some such figure.



Mr. GRÉGOIRE: Mr. MacIntosh, you say that since the bill was drafted circumstances have changed, Mr. Elderkin has presented us with a series of amendments to the bill, and in all these amendments there is not one concerning this period of transition; so it means that the Minister of Finance wants to keep this period of transition in the bill. Now, let us not discuss removing it, because the minister does not want to remove this transition period. He wants to keep it. He did not present any amendment for that. Let us speak about the bill as it stands, and not amended, because the minister does not want to amend it. You follow me? We will talk about the bill itself. According to it the ceiling would be removed only when the interest rates on short term bonds reach  $4\frac{1}{2}$  per cent. Is that correct?

Mr. MACINTOSH: That is correct.

Mr. GRÉGOIRE: And you want to see the ceiling off?

Mr. MACINTOSH: Yes.

Mr. GRÉGOIRE: When the average return on short term bonds would be at  $4\frac{1}{2}$  per cent would it be to the advantage of the chartered banks? Then there would be no more ceiling.

Mr. MACINTOSH: We wish to see the ceiling removed altogether but you have said you do not want to mix up the two questions of removing the ceiling now, which we want, and the question of its coming off when this trigger clause goes into effect at  $4\frac{1}{2}$  per cent.

If conditions existed where interest rates on government of Canada bonds come below  $4\frac{1}{2}$  per cent then you can assume that there will be a general downward shift in all types of interest rates, and this would be on both sides of our balance sheet and would, therefore, not necessarily affect our margins—I do not know; but with the ceiling gone at  $4\frac{1}{2}$  per cent, of course, it would still be possible for us to fan out interest rates. There would be some cases where borrowers would then pay more than 6 per cent because of the nature of the risk and the term. But other people might be under 6 per cent under those conditions. I am sure they will be. There will be a fanning out of rates, and, of course, we have argued there are types of risks and types of loans which we cannot now take by reason of the 6 per cent ceiling especially in the area of term loans to small businesses, which we would be able to do. It is for that reason that we want the ceiling off.

Mr. GRÉGOIRE: And know the only condition for having it off is to see the average return at  $4\frac{1}{2}$  per cent.

Mr. MACINTOSH: No; we do not want it off just to see the average return; we want it off because we want flexibility.

*(Translation)*

The VICE-CHAIRMAN: Mr. Grégoire, I will give you a few more minutes.

Mr. GRÉGOIRE: But I have not been speaking for 20 minutes, Mr. Laflamme.

The VICE-CHAIRMAN: Oh yes, you have!

Mr. GRÉGOIRE: This is going to be a pretty long process if I can't get any answer to these questions. When I am putting questions related to the Act I am answered in terms of what people would like to have in the Act, I would like to

discuss with Mr. MacIntosh what is in the Act and not what he wants to put in the Act.

The VICE-CHAIRMAN: But the questions you are putting to him are hypothetical—

Mr. GRÉGOIRE: Mine are not, they are based on the Act. Because it is directly indicated in the Act, it has not been amended by the Minister of Finance and it does not appear that the Minister of Finance does want to amend it.

(English)

The VICE-CHAIRMAN: I would like to repeat your question to Mr. MacIntosh in a more direct and clear fashion. I think he would answer and meet the same result. Once the Act has been passed, Mr. MacIntosh, what will the banks be able to do to bring about a lowering in the average yield to  $4\frac{1}{2}$  per cent?

Mr. GRÉGOIRE: That was not my question. My question is: will it be to the banks' advantage to have a lowering of this average yield to  $4\frac{1}{2}$  per cent so as to bring about the removal of the ceiling?

Mr. MACINTOSH: This is a hypothetical question, because if the interest rate were such that the level fell below  $4\frac{1}{2}$  per cent and the ceiling came off, we would like to see the ceiling off as soon as possible. We would welcome that, and there would be a fanning out of interest rates as a result of it, I would imagine. Some rates would be lower than they are now. Certainly the rates at which we buy all types of fixed assets, mortgages, securities and fixed term loans would undoubtedly fall below what they presently are at. This is a certainty. We would prefer to see removal of the ceiling under those conditions; but we would prefer, above all, to see the ceiling removed altogether now.

The VICE-CHAIRMAN: But, Mr. MacIntosh, is it in the interest of the chartered banks actually that the interest on short term bonds reach  $4\frac{1}{2}$  per cent?

Mr. MACINTOSH: You are asking me: If the bill were passed in its present form what would be the interest of the banks, from this point of view? At the present level of  $5\frac{1}{2}$  per cent plus  $1\frac{3}{4}$  per cent the upward ceiling would be  $7\frac{1}{4}$  per cent. If interest rates were to fall to  $4\frac{1}{2}$  per cent and there were no ceiling it is very difficult to say. There would be some people who would probably pay more than that ceiling of  $7\frac{1}{4}$  per cent which we would now have. What the total effect would be on the banks I simply cannot answer, because it would affect both sides of the balance sheet, under those interest rate conditions. I do not know whether our margins would widen or narrow. I cannot answer that. I do not know.

Mr. GRÉGOIRE: May I direct a question to Mr. Paton? There will be two sides to this article of the act: Either the average return of short term bonds will stay at  $5\frac{1}{2}$ , or might increase, and your interest rate will always be fluctuating, but it will be at 7,  $7\frac{1}{2}$  or  $7\frac{3}{4}$ , or the average return of the short term bonds will come down to  $4\frac{1}{2}$  and then the ceiling will be off. In your view, which is to the best advantage of the chartered banks—that the average return comes down to  $4\frac{1}{2}$  or that the average returns go as high as possible so that  $1\frac{3}{4}$  per cent plus the average return would be your interest? Which is to the best advantage of the chartered banks?

Mr. PATON: When you refer to the advantage to the chartered banks are you talking about a profit advantage?

Mr. GRÉGOIRE: General advantage.

Mr. PATON: A general advantage: Our entire thesis on this proposition is that we would like to see removal of the interest rate ceiling entirely. Failing that we would like to see it off as soon as possible. Therefore, from that viewpoint, it would be advantageous for the banks, in recognition of their desires, to get the interest rate ceiling removed to enable us to better service the Canadian public; and you must hear in mind that that is the important point, not our earning spectrum. It would be our advantage to have the average bond rate reduced to the trigger amount—hopefully, more than  $4\frac{1}{2}$  per cent—if it is the decision of this Committee and the subsequent decision of Parliament to pass the bill on this basis.

Mr. GRÉGOIRE: Thank you very much.

Mr. PATON: Does that answer your question?

Mr. GRÉGOIRE: Yes. You succeeded in answering in two minutes a question which I have tried to ask for 20 minutes. I think in future I will ask you the questions. That is exactly what I have been trying to find out since the beginning. Perhaps it is my fault. Perhaps I did not ask the right questions of Mr. MacIntosh, but that is exactly what I wanted to know.

Mr. PATON: Mr. Grégoire, it is very simple for me to come in at the end after Mr. MacIntosh has prepared the way.

The VICE-CHAIRMAN: Now, gentlemen, I will recognize Mr. Addison and then Mr. Cameron. Mr. Addison, please.

Mr. ADDISON: They ran in the first team when they ran in Mr. MacIntosh. It reminds me of a nursery rhyme about patience is a virtue, enjoy it if you can, it is seldom found in woman and never in a man!

Mr. Chairman, I would like to ask Mr. Paton this question: If the ceiling were removed now what range are we talking about, so far as interest rates are concerned, between the high and the low, bearing in mind that there will be a formula whereby the interest will be calculated in the same way in each instance and the rate will be disclosed? What would you say the high and the low would be?

Mr. PATON: I presume we are not discussing consumer finance lending at the moment but are speaking of general loans under the general loan heading on the sheet that we submitted, Mr. Addison?

Mr. ADDISON: That is right, yes. Say Imperial Oil down here and somebody else here.

Mr. PATON: Competition will control this, and any suggestion I would have would have to be an estimate.

Mr. ADDISON: Yes, that is all.

Mr. PATON: I would say that under present conditions there is no immediate possibility that the minimum rate would go below the present prime rate of 6 per cent. Therefore, I would look at that figure as the bottom of the rate structure. The top area would depend on the extent each bank individually would be prepared to take on higher risk loans. Speaking personally, I cannot visualize the Toronto Dominion Bank currently going into an area of interest rates over



possibly 8 to 8½ per cent. I think if we go back to the figures I quoted last week, where our prime rate at one time back in 1952, or 1954 was 4½ per cent, there was a range in the area of 1½ per cent. Now, this range would broaden if we had freedom, because we could take on additional risk loans, and I would hopefully think that perhaps a range of 2 to 2½ per cent would be the area in which banks would operate their normal commercial lending business.

Mr. ADDISON: I think it has pretty well been the history of the industry that interest rates, although they come down, never come down to the original level. In other words, there has been an inflationary effect in interest rates. They have always gone up. Over the next ten years obviously this is going to be the case. I am not trying to pin you down by saying that your minimum is going to be six and your top is going to be eight and a half. You know that what we consider usury now, say 12 or 15 per cent, could quite be the normal if an inflationary problem continued 10 years from now.

The thing that concerns me with this triggering device that we have is that really the chartered banks are dancing around the Bank Act as it is now, and with our consent really, because they are unable to operate, I suppose, and live with this act. If the bank rate were allowed to float free then what you are saying to this Committee is that, within the next two or three years, say, your range of rates would run somewhere between 6 per cent and 8½ per cent. In other words, we are prepared to go for 7 per cent now. Is that what we are talking about?

Mr. PATON: I would think so, Mr. Addison. I personally have not put a pencil to that particular problem.

Mr. ADDISON: Well, it is 7¼ per cent now, I think, is it not?

Mr. PATON: This would not permit us the freedom to do the job that we think we should be doing. Therefore, I say that a minimum of 6 per cent and a maximum of 8½ per cent, perhaps, would permit us to take on these additional areas of lending that we feel we are being prohibited from doing now. I think that is a reasonable ratio in line with banking history from long ago. We are not going to extend credit to a risk beyond what is normal for a bank lending operation.

Mr. ADDISON: In the last ten years, then, that means that some people were borrowing money at 3½ per cent, I suppose; is that right?

Mr. PATON: No, not in the last ten years. The prime commercial lending rate of April, 1956 for example, was 5 per cent.

Mr. ADDISON: Yes; but in some instances would you not go below that?

Mr. PATON: That would be the prime commercial rate and would include some secured loans, too. Your loans against the security of government of Canada bonds would be fractionally lower than that. But that would be the best rate to the great majority of general loans on the banks' books.

Mr. ADDISON: I am not trying to pin you down to an 8½ per cent figure.

Mr. PATON: No, I would not wish to be.

Mr. ADDISON: I appreciate that. We are speaking roughly of between 7¼ and a high of 8½ which you are suggesting, perhaps.

Mr. PATON: I think so. Would you agree with that, Mr. Coleman?

Mr. COLEMAN: Yes; I agree with what Mr. Paton says, Mr. Addison; but, as you know, banks do not determine the level of interest rates. The market forces of the world play a very important part in this, but given no change in monetary conditions, assuming—and I think this is what you are asking—that monetary conditions remained about the same as they are now, what would the level of interest rates be? I would agree with Mr. Paton that the spread could be 2 to 2½ per cent.

Mr. ADDISON: You are saying really that this triggering device will not take place in the next three years?

Mr. COLEMAN: It would appear this way, yes.

Mr. ADDISON: So we are speaking of between 7¼ and the rate you are talking about.

Thank you, Mr. Chairman.

The VICE-CHAIRMAN: Mr. Cameron?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Chairman, I wonder if, without any disrespect to these gentlemen at the table, I might put my questions to Mr. MacIntosh. I notice that you call on him when you want answers to the sort of questions I am going to put. They are not like Mr. Grégoire's questions and they are purely a search for information, Mr. MacIntosh.

There have been a number of references—in fact one was made a moment ago by Mr. Coleman—to the effect of world interest rates on our domestic rates in Canada. What I would like to ask you is this: I can understand how, in particular with regard to United States interest rates, we are obliged to keep our interest rates in Canada higher than the American interest rates if we hope to be able to attract the sort of borrowing that many of our provinces and municipalities have to undertake, for instance, and that the influence of international rates is such that it will keep our interest rate up. Can you tell me if there are any international pressures, or influences, that would tend to keep our rates down?

Mr. MACINTOSH: Mr. Cameron just after being told by Mr. Grégoire that I was unable to answer him I am not very optimistic about being able to answer you.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Maybe I am more easily pleased.

Mr. MACINTOSH: I hope so.

I cannot think of any forces now at work which are tending to ease interest rates other than the possibility that deflationary measures in the United Kingdom might eventually spill into world markets; but this is a quite distant and difficult thing to assess.

I think it would be generally agreed by most economists and observers that the demands for capital throughout the world are high and rising; the unsatisfied demand from underdeveloped countries for capital is almost unlimited; and the developed countries of the world, whether it be in North America or Europe or Japan, have been coping with such high rates of technological change, and with such high requirements for capital investments internally for social capital purposes, that I would think nearly all the forces are tending to be on the side of holding interest rates up. Even in the United Kingdom, where the rate of growth

has been slower than in this country for ten years or more, ever since the war, and where the present government, I think, is not really biased in favour of high rates, it would be true to say that their rates are higher even today, with some kind of recession coming into their economy than here.

Therefore, in summary, I would not think that, at the moment, there are any strong forces working towards the lowering of interest rates.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Could I ask you what, I admit, is purely a hypothetical question: If conditions should arise whereby Canada became less dependent on the United States for the provision of capital, so that it was reduced to very minor proportions, would there be any influences on the Canadian economy that would force our interest rates up to the level of world rates?

Mr. MACINTOSH: Well, let us try to separate the short run from the long run.

In the very long run, if income and wealth in Canada rise to American standards of living I would except that our level of interest rates would generally fall towards theirs; and if that is what you mean by forces working towards lower interest rates I would say that ultimately a country with a high level of economic development, even with a high rate of growth, would have a lower level of interest rates than an underdeveloped country. If you look at a country like India, there rates of 24 and 50 per cent are common, as they are in parts of South America, where you get a really extreme case.

However, if you mean that further development of the country would tend to bring us closer into word markets as far as capital movements are concerned, I would say that we are already very much part of the world capital market. The world has suddenly become very small in the last ten years in this respect, with the freeing of exchange transactions and capital transactions, and we are very much a part of the world market. Money flows from Canada to countries abroad, and, of course, if flows inwards mostly from the United States but not entirely so. Canada helps to finance underdeveloped parts of the world. There was a world bank issue last week in Canada which is financing underdeveloped countries.

I would say that our present development and our future development both leave us closely related to world capital markets and that we cannot isolate ourselves from them. We are part of them.

The central bank can do certain things, in the short run, to cushion us, or to isolate us, from short term capital movements, and they do that today. In fact, if you look at our treasury bill rates in Canada, they are below the United States, treasury bill rates at the moment, which is unusual; so that it is not always the case that rates in Canada are above American rates in the short run.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then, Mr. MacIntosh, would it be fair to say that if—and Mr. Paton has told us that this is what the banks would like—the 6 per cent ceiling were removed immediately, there are no international perssures which would keep interest rates in Canada down?

Mr. MACINTOSH: Yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): That would be correct.

Mr. MACINTOSH: I think so; at the present time, yes.

Mr. COLEMAN: Do you mean at the present time, or are you speaking hypothetically?



Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well, I am speaking of the present time and the next several years.

Mr. MACINTOSH: My answer would be yes. And, of course, our view is that we should not be left in this position of being isolated in our lending operations from conditions which exist not only elsewhere in Canada but everywhere else in the world and in other banking systems which have this rate ceiling business.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I am not sure that you quite understood my question. There was a suggestion, it seems to me, once or twice in these hearings, that there were international forces which, we will say, would prevent the chartered banks from going hog wild and raising their interest rates sky high. Now, am I right in saying that you are of the opinion that there are no international forces that would prevent this happening?

Mr. MACINTOSH: Well, I think there are plenty of forces. That is a different question from your other question. Your first question was: Are there international forces which would lead to a decline in rates in the near foreseeable future, and my answer to that was No. But if you say: Are there international forces which would prevent us charging sky high rates, certainly there are.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): That is what I wanted to know.

Mr. MACINTOSH: There are, certainly, yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): What are those forces that would do that?

Mr. MACINTOSH: If our rates were sufficiently high, of course, it would produce a deflationary effect on the Canadian economy, and deflation of the Canadian economy would quickly have international effects on our imports and exports, on our capital relations with the United States and on our exchange reserves. More than that, some borrowers would be driven abroad if our rates were—to take a preposterous case—let us say, 10 per cent for loans, so that corporations virtually could not borrow here. If our rates were so high then they would not be able to borrow in our open securities markets, either, presumably, because rates would be comparably high. They would borrow in New York, or elsewhere. This would set up capital inflows from abroad which would create severe problems for the central bank.

On the aspect of our exchange reserves, we have certain commitments to the Americans now, and it would involve the totality of our economic policy, I am sure.

I think, even without looking abroad, that if the rate ceiling is removed we are still subject, even internally, in Canada to all sorts of competitive forces which would prevent our charging what the traffic would bear. Certainly, for instance, in the mortgage market there are very many lenders, and we would be only one of many well-developed institutions and not in a position just to charge anything we wanted. We would have to go by the market.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): What you are saying is that the forces which would control us are, in the main and fundamentally domestic forces.

Mr. MACINTOSH: Yes, I think that is correct; in the main, domestic, but you cannot ignore the foreign ones.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well, I still have not got it clear whether there are any foreign influences that could keep our rates down. I wanted to get this cleared up, because there have been several sorts of suggestions that in the final analysis we are protected in the chartered banks because of the forces of international interest rates. I would like to know how they work. It seems to me that our main considerations must be domestic.

Mr. MACINTOSH: There would be capital influence from abroad, nevertheless. You have asked: Are there presently visible forces which would cause rates to fall? I think not. But it is a different thing to ask: are there forces in the international market which would prevent interest rates from going unreasonably high? I say, yes, there certainly are such forces. There would be capital inflows. There would be attempts to borrow abroad.

The VICE-CHAIRMAN: You have a supplementary question, Mr. Lind?

Mr. LIND: My question has to do with the weekly price of treasury bills that are purchased by the chartered banks. Does the American money market have any influence on what the government receives for these treasury bills?

Mr. MACINTOSH: Mr. Lind, the short answer is yes; this is one of many factors; but it is possible to isolate to some extent the Canadian treasury bill market from the United States treasury bill market because of the forward and spot exchange rate and the operations of the central bank in that market.

Ordinarily United States treasury bill rates are lower than our rates. At the moment, they are higher. The reason it is possible for them to be higher than ours now is that the difference between the spot and forward exchange rates in the market make it impossible for short-term investors to move money from Canada to the United States and buy United States treasury bills advantageously. This is true for the banks right now for market reasons. That is to say we cannot buy United States bills using Canadian dollars and buying U.S. and selling them forward 90 days without incurring a loss in the yield which would make it not worthwhile. Besides which, the Canadian banks are required to hold 7 per cent of their deposits in secondary reserves, so that we are to a large extent a captive market for treasury bills in Canada.

Mr. LIND: Is it not true that last year, when the United States suddenly raised their rate of interest by 1 per cent, we in Canada immediately raised our rate to avoid a drain?

Mr. MACINTOSH: It is generally the case that if the board of governors of the federal reserve system in the United States are raising the discount rate and taking monetary actions which have the effect of raising interest rates in the United States, these would very definitely tend to spill into Canada. But it can get complicated by reason of this exchange market.

Mr. LIND: Is it not true, Mr. Chairman, also, that the interest rate has been decreasing a little bit of late in the United States, and that we might just be on the peak where we are balancing over to enter the downswing?

Mr. MACINTOSH: I think, Mr. Lind, it would be premature to say that. United States treasury bill yields are around, if I remember correctly, about 5.44 to 5.55 per cent at the present time compared to ours which is down to  $5\frac{1}{8}$  per cent level; and I see no indication yet that United States yields are easing at all.

Mr. LIND: Thank you.

The VICE-CHAIRMAN: Now, I will recognize Mr. Fulton.

Mr. FULTON: Mr. Chairman, I have been sitting here for two weeks or more with a series of questions that I wanted to ask the Bankers Association and Mr. Paton. I was about a quarter of the way through when the Committee decided it would deal with specific matters and we have been dealing since with interest rates generally. I have only an incidental question on interest rates. Perhaps I could ask it now, but I just want to make it clear that I have a number of other questions.

On interest rates, Mr. Paton, is it correct to say that, generally speaking, bank profits are a reflection of the difference between the interest rates paid to depositors and that which you charge to lenders? Is that the main factor in determining bank profits?

Mr. PATON: That is where the major part of our revenue comes from.

Mr. FULTON: You may have dealt with this before and, if so, my question is disposed of: In setting rates, because banks must operate at a profit, do you take into account profits that might be derived from other related activities in which the banks participate, even what might be called strictly non-banking activities? In other words, if you can foresee a profit coming from some other enterprise which is not strictly a bank enterprise but which, nevertheless, accrues to the bank, would this be taken into account in setting the level of interest rates you charge? Do you set your potential over-all profit picture and let it have a bearing upon the interest rates you charge?

Mr. PATON: My answer to that would be no, Mr. Fulton. I cannot conceive of an important enough revenue in any ancillary operation of a bank that is not directly a part of the banking operation.

Mr. FULTON: I have in mind not only the operations of RoyNat and Kinross as the two prime examples, but your very substantial real estate holdings. The Royal Bank has the Place Ville Marie, am I right? And there is your Toronto Dominion centre. I realize in the over-all picture of gross revenues they would still be minimal, but I am trying to get a general answer based on some specific examples. In other words, to the extent that banks do go into other forms of activity which may be closely related to banking, or may not, as a real estate operation, be really banking at all, could this have an effect, by its reflection on the over-all profit of the whole bank, on the interest rates you charge?

Mr. PATON: Mr. Coleman has suggested that he would like to interject.

Mr. COLEMAN: I would say, Mr. Fulton, that the interest rate is in a separate compartment completely. The rate is dictated by the cost of money and the quality of the risk. While I am here I want to say that we have no income from the Royal Bank Building in Place Ville Marie. We do not own it. I thought I should clear that up.

Mr. LAMBERT: Surely, though, in the competitive field the long range look is to the consolidated operations of the bank. I think this is what Mr. Fulton is getting at; that, coming down to the crux of a real competitive situation, and bearing in mind your relationship with your shareholders and all of this, your



consolidated operations are not neglected in determining the level of interest that you may pay to savings depositors or that you may charge to borrowers.

Mr. COLEMAN: I was thinking exclusively of debit interest rates, and I thought you were referring to that. I was referring to interest rates on loans, not credit interest rates.

Mr. FULTON: But you have to take them both into account when you are considering your profits.

Mr. PATON: That is correct, Mr. Fulton. The over-all operations of each bank are taken into consideration in our budgets. We all have budgets. We have just recently completed our fiscal years for 1966 and we are currently, I would be sure, employed in budgeting for our operations going into 1967. It is difficult, not knowing the exact circumstances under which we will be working, but there is no question, in any well operated bank, that we project budgets and anticipate what our earnings situation is going to be next year, and all the avenues of revenue are included in this budgeting process; however these are not directly related to interest rates.

Once the 6 per cent ceiling is non-existent then interest rates will fluctuate to an even greater degree. We will constantly be concerned about the margin between what we pay and what we get, and we will have a certain constancy in the differential between the two. Basically that would be the basis on which we would act.

Mr. FULTON: Yes; but in the over-all picture, if you were deriving substantial profits from other operations, is it not reasonable to suggest that you would be prepared to operate on a narrower margin than you would if the process of borrowing or lending is your only source of revenue or of profit? I should not say borrowing—if the process of receiving deposits and making loans were the only source?

Mr. PATON: In a competitive operation, Mr. Fulton, there is no question that the individual rates set by each bank for each will be affected by their over-all operations.

Mr. FULTON: I am sure you will appreciate that I am referring to that portion of the bill, as it stands now, which requires the banks to divest themselves down to 10 per cent of the shareholdings in other companies. My question is to some extent hypothetical, but I think it is important, and that is why I am asking you whether the potential profits to be derived from these related operations would not have some effect on the margin between what you pay depositors and what you charge to borrowers? Is that a reasonable assumption?

Mr. PATON: Looking ahead that could be a reasonable assumption. I might interject also that, while we have heard the names of Roy Nat and Kinross mentioned frequently at these hearings, there are other similar corporations, in which other banks have interests, that are equally applicable.

Mr. FULTON: Do we have a list of all those who would be affected by that provision in the bill?

Mr. PATON: No, sir.

Mr. FULTON: Would there be any objection on your part to giving us that?

Mr. PATON: This is perhaps digressing somewhat from the ceiling rate, but there was a suggestion earlier on, when Mr. Elderkin was on the stand, that the banks would produce this information—the names of the companies, the number of shares owned and the percentage. This question has not come up since the Bankers Association appeared before the Committee, but we have done some thoughtful study in this connection.

We would like to go on record to the following effect, that, although we recognize that the Committee desires to obtain all information pertinent to the consideration of the bill, we feel that there is an aspect of the matter, to which the Committee would wish to give careful consideration, and that is the question of disclosing these particulars. The policy of the present Bank Act is quite clear. Under section 63(3) the Inspector General has the right of access to the securities held by a bank, and the bank is bound to give him all the information he requires in any matter connected with the performance of their operations. Section 67 prohibits the Inspector General from disclosing this information to anyone, save the Minister, the Deputy Minister or the governor of the bank, or his authorized representative.

With these limitations, Parliament has determined that it is not expedient to make public such information regarding the affairs of the bank, and similar provisions to the ones I have commented on are in the present Bill No. C-222.

We feel there are sound reasons for this policy and it is not too difficult to see just what some of these are. For example, it might be expected that a disclosure would have an unsettling effect on the securities market. The disclosure might amount to giving information regarding the affairs of the customer, contrary to the well-recognized duties of a bank. A certain bank might have ownership of shares as a result of an arrangement with a company for the purpose of preventing it from falling under foreign control. The basis for the acquisition of shares in a number of these companies will vary, but this is one example, where it might be detrimental to have this information made public.

On the whole, the banks feel that such a disclosure would not be consistent with their responsibilities to their customers, and would like to be sure that this Committee would not wish us to give this information unless the Minister, to whom the information is already available, proposes to suggest a change in the established policy of the act.

I have adhered fairly closely to the statement that we prepared on this subject, in general, and I would find it rather difficult to give even a list of names, even if specific information was not included.

Mr. FULTON: Mr. Chairman, we have come to this question of these other corporations by way of questions on the interest rate, and I think perhaps it would not be in keeping with the decision of the Committee right now to go into the matter while we are still on interest rates. Indeed, I would like to go into this matter as a separate area of questioning and—

Mr. PATON: It is in our brief as a separate item.

Mr. FULTON: —therefore, I would like to suggest, at least for myself, that we withhold any further request for this information until we have a chance to consider the implications of what Mr. Paton says.

In so doing, and at the moment retreating from this line of questioning, I feel that it is going to put us in a difficult position, in passing a judgment upon the new proposal in this bill about divesting yourselves, unless we know the extent of the effect of this requirement. Unless we know some of the information that you are reluctant to disclose, then we are going to be guessing in the dark. That is why I would like, for myself, to consider the matter further before returning to this particular line of questioning.

I think I have completed my questioning on the possible relation between interest rates and the interests of banks in other corporations. If you prefer that the Committee confine itself to interest rates, I will have to defer further questioning.

The VICE-CHAIRMAN: Yes; that is not necessarily the consensus of the Committee, but since I have two more members who wish to ask questions on interest rates, I think it would be preferable to go on with interest rates.

Mr. Thompson, you are next.

Mr. THOMPSON: Mr. Chairman, I would like to ask Mr. Paton a few questions arising out of an answer that he gave to Mr. Grégoire, and I have some questions which come to my mind out of a recent article which Mr. Paton has written, which appeared in the April 11, 1966 issue of the *American Banker*.

Do you consider the chartered banks to be a service-rendering facility, intended to facilitate money which makes possible the exchange of goods and services and the development of resources, or do you consider the banks to be a facility dealing mainly with money as a commodity, with the basic motive of making a profit?

Mr. PATON: In line with the testimony I have given in the past few days, Mr. Thompson, the basic premise under which we operate—and I think we have certainly contributed to Canada's growth by our operations—is to facilitate the manufacture, exchange, sale, and purchase of goods, also our import and export trades, primarily; and the result of the first part of your question would automatically produce the effect suggested in the second part.

Mr. THOMPSON: That is a very noble definition.

Mr. PATON: I do not think I said that in the April issue of the *American Banker*.

Mr. THOMPSON: It is quite legitimate; but would you say that the desire to increase interest rates at this time is because the profits of the banks have been too small?

Mr. PATON: No, sir. Our main premise on this whole operation is that we have a job to do, which we cannot do properly. We will eventually increase our earnings as a result of more freedom to operate, and this, I think you will agree, is a very laudable purpose to reward our shareholders for their confidence in investing in our operations.

We would hope—and I think I may be paraphrasing what the Minister of Finance said when he appeared before us at a dinner we had in June last—that we would gain greater earnings from maximizing our business and making our operations as efficient as possible. This would result in increased earnings for the banks.



Mr. THOMPSON: Do you have statistics on hand which would give us the increase in assets—which would include profit—of the banks in 1964 and 1965?

Mr. PATON: Yes, sir, we have that information. Would you like the total assets in the banking system?

Mr. THOMPSON: The total increase in assets for 1965 over 1964 and 1964 over 1963.

Mr. PATON: On December 31, 1964, the total assets of the chartered banking system were \$23.871 billion. The comparable figure in 1965 was \$25.875 billion, roughly an increase of \$2 billion.

Mr. THOMPSON: I think we usually regard the banks of Switzerland as being the money depositories of the world. I find that their profits for the same period of time were approximately one-eighth of that.

Mr. PATON: These are not profits.

Mr. THOMPSON: I should say their increase in assets—approximately one-eighth of that amount. The total increase in assets between 1964-1965 in the banks of Switzerland—if my figures are correct—was \$295 million.

Mr. PATON: What was the starting figure, Mr. Thompson?

Mr. THOMPSON: I do not have those statistics before me.

Mr. PATON: Percentagewise, is there a difference?

Mr. THOMPSON: Yes; there may be not as much as far as the total assets are concerned, but percentagewise there is quite a difference. My reason for asking that comes back to the previous question: Are we attempting to increase the profits of the bank, or are we attempting to increase the facilities of the banks?

Mr. PATON: This increase in banking assets, of course, is beyond the control of the banks. The central bank of Canada operates the money supply in the country and dictates what the total supply will be. The banks acquire their share of any increase in such money supply total.

The VICE-CHAIRMAN: Mr. Thompson, if you do not mind, I would ask that this Committee adjourn until 3.45 this afternoon, and at that time you may continue your questioning.

Mr. THOMPSON: I would like to ask one very brief question of Mr. MacIntosh. It arises from your statement of a moment ago, that the world bank last week made it possible for Canada to issue a number of development loans, or loans to developing countries. What was the rate of interest charged on those loans?

Mr. MACINTOSH: Mr. Thompson, it was a borrowing by the world bank in the Canadian market, and I believe the coupon rate was about 6.40 per cent.

Mr. THOMPSON: And that was for the purpose of loans which were to be made to developing countries?

Mr. MACINTOSH: Yes, sir.

Mr. THOMPSON: Do you know what is charged on these loans by the world bank?

Mr. MACINTOSH: Their rates are usually in line with competitive banking rates for the purposes involved. I cannot tell you what their actual rate of return is, but I am sure we can get that.

The VICE-CHAIRMAN: We will resume our sitting at 3.45 this afternoon.

*(Translation)*

Mr. GRÉGOIRE: On that adjournment suggestion, since there is a vote in the House at 8:30, will this evening's meeting of the committee take place anyhow? We are dealing with an amendment to the motion to go into supply.

The VICE-CHAIRMAN: As soon as we resume, we will have an opportunity to discuss that and we will see whether it is possible for us to sit this evening in spite of the vote.

Mr. LAMBERT: I think it would be in order for us to sit to-night. The vote will take only a quarter of an hour or twenty minutes, at the beginning. We could resume our sitting later. These gentlemen have come here at their own expense, not at ours.

Mr. GRÉGOIRE: But supposing there were an amendment to the amendment?

## AFTERNOON SITTING

*(Recorded by Electronic Apparatus)*

TUESDAY, November 22, 1966,

The CHAIRMAN: Well, gentlemen, we can now resume our session from this morning.

I am informed by the clerk that when the meeting recessed Mr. Thompson had the floor and I would invite him to continue at this time.

Mr. THOMPSON: Thank you, Mr. Chairman. My questions will be few and brief.

I wish to ask Mr. Paton for a few statistics. What was the aggregate of customer deposits held by the chartered bank system in 1965?

Mr. PATON: The total deposits of the chartered banks in Canadian and foreign currencies as at December 31, 1964, Mr. Thompson, was \$21,908,000,000.

Mr. THOMPSON: Could you give me the—

Mr. PATON: The breakdown?

Mr. THOMPSON: No, that is not necessary. Could you give me the total aggregate loans during the same period?

Mr. PATON: The total of all loans, exclusive of loans invested in the day to day money market, in 1964, was \$12,439,000,000.

Mr. THOMPSON: What was the average daily cash reserve ratio during that same period?

Mr. PATON: I hope you will not hold me to the point but it would be roughly around 8.05 I beg your pardon. Here we are. The monthly average in 1964 was 8.14.

Mr. THOMPSON: Am I correct then, Mr. Paton, in saying that, according to these statistics, the banks were actually lending the maximum of their capacity under the reserve requirements of the Bank Act?

Mr. PATON: No, that is not a correct conclusion, Mr. Thompson. The 8 per cent is related to our deposit liabilities, not to our loans. Deposit liabilities are invested in securities and loans.

Mr. THOMPSON: Well, am I right in saying, then, that the deposit liabilities were practically at a maximum?

If your reserve requirement is 8 per cent and you are operating at 8.14 you are practically at that point?

Mr. PATON: That is a constant figure, actually. The 8.14 is derived from the total deposit liabilities of the banks.

Mr. THOMPSON: Would it not be correct to say, then, Mr. Paton, that increasing the interest rate is going to do little for the banks in extending their ability to become more competitive, on the basis that you are already operating at maximum as far as your loan and deposit liabilities are concerned?

Mr. PATON: No, that would not be correct.

Mr. THOMPSON: Would you explain why it is not correct?

Mr. PATON: Removal of the ceiling would enable us to attract additional deposits. Attracting additional deposits would enable us to make additional loans.

Mr. THOMPSON: Do not your loans depend upon the reserve requirements?

Mr. PATON: No, sir, not on the reserve requirements; the 8 per cent reserve is against our deposit liabilities, which is the other side of our ledger.

There is no fixed ratio, other than good judgment, between loans and the cash reserves.

The CHAIRMAN: Mr. Thompson, do you wish to yield for a brief supplementary question?

Mr. THOMPSON: Yes, for a supplementary, if it is on this point.

Mr. GRÉGOIRE: Can you accept deposits when you do not have an 8 per cent cash ratio behind it? Suppose you have \$1,524,000,000 cash reserves, which is an average of 8 per cent of the \$18,855,000,000 you had in September 1966. If you were adding deposits, and suppose that you increase the interest; you bring in \$1,000,000,000 deposits and you do not increase your cash ratio. That will bring down your cash ratio to 7 per cent. Would you be entitled to do that?

Mr. PATON: Mr. Grégoire, you are back to a point on which I would like to suggest that I recall Mr. MacIntosh. I am not too sure that that would meet with your approval, but I would like to reserve my strength and fortitude for some questions with which I am more familiar.

The CHAIRMAN: I have a great deal of confidence in the strength and fortitude both of Mr. Paton and Mr. MacIntosh, but at the same time I think we are getting into the general area of reserves and this is the topic following this one in due course.

Mr. GRÉGOIRE: No, Mr. Chairman, it is completely in line with questions that he has been asked, because this increasing interest would increase their deposits.

The CHAIRMAN: Yes.

Mr. GRÉGOIRE: And I have asked him if he can increase his deposits when his cash reserves do not increase?

The CHAIRMAN: Your question arises out of Mr. Thompson's.

Mr. GRÉGOIRE: Yes.

Mr. THOMPSON: My point is that, as far as the banks are concerned, in increasing their ability to render a service—and I am coming back to your own



definition again, both in the April article and in your statement today—is it not important to the banks that the reserve ratio be changed rather than to increase your rate of bank interest, in so far as extending your service is concerned.

Mr. PATON: No, sir. These changes, reserve rates vis-à-vis interest rate, are not related in the context in which you are discussing them at the present time, Mr. Thompson.

Mr. THOMPSON: I am speaking of service to the public, and I am relating it to the proposal to lift the ceiling on interest rates.

Mr. PATON: If the ceiling is removed and we attract additional deposits 8 per cent of these deposits have to be left with the Bank of Canada free of interest. It is a constant-revolving, constant-moving amount. It is not a question, with certain stipulations, as Mr. Grégoire stated, of one item which is movable and another which remains constant, thereby getting back to the 7 per cent he was referring to. Automatically we have to provide the reserve against any deposit. If you come into my bank and deposit \$100 with me, \$8 of that goes to be lodged with the Bank of Canada. You cannot have deposits changing and reserves remaining stationary.

Therefore, the removal of the interest rate ceiling will be the weapon—well, “weapon” is not a good word—will be the medium through which we can go out and attract deposits, and then the next step, or concurrently with attracting deposits, our reserves must be adjusted to meet these totals.

Mr. THOMPSON: It is a question of which came first, the chicken or the egg?

According to your reserve requirements it does not relate in the first instance, as I understand it, to your deposits; it relates to your actual ability to loan. Therefore, it is more important, as far as the service facility rendered by a bank, that your reserve ratio be changed than it is to raise the interest rates.

Mr. PATON: No, no, sir.

Mr. THOMPSON: As it stands now, you are not operating at maximum capacity as far as the present reserve ratios are concerned. No matter what the interest rates are, you are not going to be able to extend your facilities unless you are able to increase your deposits with the Bank of Canada.

Mr. PATON: Unless we are able to increase our deposits from the public, i.e. our deposit liabilities, from which automatically our deposits with the Bank of Canada are adjusted.

Would Mr. MacIntosh be able to clarify this any better, or, shall I say, clarify it at all?

Mr. MACINTOSH: Mr. Chairman, I am afraid I have already overstayed my welcome at this Committee.

I think we are entering an area of discussion which we considered last week when Mr. Johnston was asking some questions.

Mr. THOMPSON: As it relates to the increased cost of money.

Mr. MACINTOSH: Well, one problem would be the reduction of the cash reserve ratio, and the other one would be the effect of removing the interest rate ceiling. If you asked: Would not the effect of reducing the cash reserve ratio be more advantageous to us than removing the interest rate ceiling, I think I would

have to answer that it would probably not be of very much advantage, in the first instance, to have the cash reserve ratio down, because the central bank would more than likely offset the lower cash reserve ratio by sopping up the cash difference through its open market operation. In other words, if you bring the cash reserve ratio down from 8 per cent to 6.6 per cent, which would potentially free a large amount of cash reserve—1.4 per cent of deposits—the central bank, unless it wishes to create a very inflationary situation, would certainly not leave that cash rolling around in the system. They would go into normal central banking operations and mop it up, so that we would probably end up with a lower absolute amount of dollars of cash reserves, or a lower cash reserve ratio, and the same deposits.

Mr. THOMPSON: What relation is that going to have then to increasing interest rates?

Mr. MACINTOSH: They are really unrelated, and the object of reducing the cash reserve ratio was to put us a little closer on a footing with the near banking institutions which have somewhat lower cash reserve ratios, and who, moreover, are able to earn interest on their cash reserves because they keep their cash reserves—and I am speaking now of the trust companies, the loan companies, and the other near-banks as described by the governor of the Bank of Canada, the credit unions and *caisses populaires*—these institutions all keep their cash reserves with other chartered banks, and they get interest on those reserves, and they keep a lower ratio of reserves. They keep perhaps only 4, 5 or 6 per cent to our 8 per cent, and the object of reducing our ratio from 8 to 6 was to remove some of the disadvantage that we suffer from in having a higher ratio of non-earning assets.

Mr. THOMPSON: Now, the statement you have just made there is contradictory in that you have said that it is not going to place you at an advantage.

Mr. MACINTOSH: Well, not in the first instance, otherwise the effect of changing the act would be a gross inflation, and I am sure that the central bank would not do that. Ultimately, it would lead to a shift of our assets from an 8 per cent cash reserve ratio to 6.6 per cent cash and 1.4 per cent other assets, which could very well be not just loans but partly secondary liquid reserves including government of Canada securities. It would not follow that the whole 1.4 per cent would end up in loans. Part of it would, I suppose, ultimately.

Mr. THOMPSON: I am afraid we are getting into another area here, Mr. Chairman, and I will just leave it until we start discussing other matters on the subject of mortgage lenders.

Mr. LAMBERT: Mr. Chairman, I want to follow up on something that Mr. Fulton was discussing this morning, and that was the statement by Mr. Paton and Mr. Coleman that the bank deposits depended upon the spread between the net cost of money to them and the net revenue they made on loans, and that that really was the principal source of the profit on their operations, and that ancillary business conducted by the banks was of no concern, or of no importance, in determining the rates of interest either paid or collected. However, I would put it through you, Mr. Chairman, to either Mr. Paton or to Mr. Coleman, that, essence, the directors of a bank cannot ignore the complete picture on the bank's consolidated operations when they are determining the interest rates that they will pay on savings deposits or on deposit certificates and the interest rates

that they will charge to their loan customers; because it seems to me—and I would like your comments on this—that the wider the base of operations of a bank the less reliance it must place on one source of profit, for flexibility, and that if the prime concern of the banks today is competition, therefore, they must insist on as wide a base as possible in order to diversify and that, in the essence of competition, the more they can narrow that gap between the net cost and the net return on funds the more competitive they are going to be.

Therefore, I would like you to think again about the statement you made. Would it not be truer that you must really look at the consolidated operations of the banking system when you are of a competitive nature and have a desire for competition.

Mr. PATON: The point, Mr. Lambert, is well taken, that we do consider the entire picture when we are looking at our position for the year past and anticipating what it will be for the year to come.

These ancillary operations which we are referring to and which are referred to in Bill C-222, are relatively recent. They are the result of planned investment by the management of individual banks with a view to providing a service that is not already fully covered by existing agencies and also with a view to having a profitable operation. That is correct.

We would be remiss in our duties as management of the banks if we were to invest in any such company purely for philanthropic purposes. We have to consider the profit picture, but, at the same time, to associate the earnings from these sources as of today specifically to an interest rate that is paid by us to our depositors, or charged by us to our borrowers, would not be factual, would not be realistic, simply because the net revenue from our interest earnings are substantially greater than any revenue that within reason we can net from these new companies with which we have become associated.

We would also hope that as time goes on the influence of these companies in relation to our total would increase. This is one of the objects of the exercise. But even looking ahead to the time of the next revision, I think it would be inaccurate to say that the earnings from these sources would have a noticeable effect on the interest rates that we would be assessing or paying. I think the important part, towards the continuation of legal permission for us to get into enterprises of this nature, goes beyond the question of the effect it would have on interest rates. It goes into the area of enabling us to develop our operations and to get into services that presently we are not in. We want permission to continue to do as we have done namely invest in companies we have helped to form, or in existing companies. These were all entered into under the proper aegis of the Bank Act under which we are operating.

To sum it up, I would be very hesitant to suggest, that the earnings from our ancillary operations would be consciously in our minds when, with competition free and no ceiling, we were deciding what interest rates we would allow on our various depository certificates, or our savings accounts, the interest in all of which would be subject to much more frequent fluctuations than they have been in the past. Market conditions would evolve at a considerable greater velocity than they have in the past.

Mr. LAMBERT: Well, are you suggesting therefore, that the thesis that I have put forward, of the consolidated operations not affecting your competitive na-



ture, or your competitive position with regard to the interest rates either that you will pay to depositors or that you will charge to lending customers, is not valid? I want to be sure, because it seems to me that you have walked up to it to accept it and then backed away.

Mr. PATON: I think my concern was that I might leave with you the impression that this would have a much more material effect in this area than I can foresee, looking at it as it now is.

Mr. LAMBERT: Well, I would suggest to you, Mr. Paton, that it would be highly desirable that the banking system be more flexible by not having such a great dependence for its successful operations in that one narrow sector. True enough, it is a big one, but it is limited in its ambit, but you would be far more competitive if you had a broader base for operations.

Mr. PATON: We agree with you one hundred per cent. This is our philosophy. We do want to have a broader ambit.

Mr. LAMBERT: All right.

Mr. PATON: And I will admit to you quite freely that the earnings from that broader ambit are bound to have an impact on our judgment. I feel however I would be remiss in leaving you with the idea that it might make a difference of any specific percentage.

Mr. LAMBERT: Oh, no; what I am suggesting is that it does affect your thinking. In many instances, the banks are in business like a merchandising concern, or a contracting firm, and you might be prepared to take on a loan or take on a deposit at, shall we say, a somewhat more favourable rate for good and valid reasons providing you have this more extensive cushion of earnings elsewhere. In other words, as in the merchandising business, you might be prepared to do a bit of loss-leading with certain operations. Well, perhaps I should not say loss leading, in that sense—the term is a little more favourable—but that you are in there for reasons of good business, just as a contractor is prepared to go in and tender at a rate that will cover his expenses and just a little bit more, because for the general conduct of his business it is highly important that he stays there.

Mr. PATON: I would agree. I think there is not a great deal of difference in your suggestion and my philosophy, Mr. Lambert. Undoubtedly, the more enterprising banks—assuming they have the freedom to move—will have additional facets to their operations which will enable them to perhaps be more competitive and to be more efficient in their operations.

Mr. LAMBERT: Thank you, Mr. Chairman, I think we can develop this further under the section of the brief dealing with the disposal of subsidiaries.

Mr. GRÉGOIRE: I have just a few brief questions of a general nature concerning the interest problem.

Mr. Paton, as we can see, there is about \$2,500,000,000 of Bank of Canada notes generally and globally. Is that right?

Mr. PATON: I will accept your reading of—

Mr. GRÉGOIRE: An average of \$2,500,000,000, is that right?

Mr. PATON: You are reading from the Bank of Canada figures here?

Mr. GRÉGOIRE: Yes?

Mr. PATON: I will accept them.

Mr. GRÉGOIRE: \$2,598,000,000, let us say \$2,500,000,000.

Mr. PATON: Bank of Canada notes.

Mr. GRÉGOIRE: Notes in circulation—the total. Now, we see also that the chartered banks have cash reserves of \$1,534,000,000, is that right, out of which there is \$1 billion on deposit with the Bank of Canada, and about \$500,000,000 in all chartered banks, which is regularly circulating. It means an average of \$90,000 per branch. The other \$1 billion of Bank of Canada notes are circulating among the public? Is that right? That is the disposition, in general, of the Bank of Canada notes.

Would you agree that out of \$5 of Bank of Canada notes put into circulation by the Bank of Canada, an average of \$3 are going to the chartered banks as a cash reserve, and \$2 are going to the public, or into regular circulation? Would you agree that that is the general percentage?

An hon. MEMBER: What has this got to do with interest?

Mr. GRÉGOIRE: I will come to the interest. This is just preparatory.

The CHAIRMAN: The road you are travelling by way of preparation should not be too long.

Mr. GRÉGOIRE: No, no.

Mr. PATON: I am finding it very uphill.

I will concede, Mr. Grégoire, that if, as you say, of the \$2½ billion Bank of Canada notes \$1½ billion is in possession of the banks, then \$1 billion must be in the possession of the public and other financial institutions.

Mr. GRÉGOIRE: Now, you say that they are in the hands of the other institutions. Mr. MacIntosh said, in answer to Mr. Thompson, that cash reserve of trust companies and finance companies are deposited in the chartered banks.

Mr. PATON: Mr. Grégoire, I think, we are not in empathy on, that we are not batting on the same wicket—The Bank of Canada notes, in so far as the chartered banks are concerned, are a part of our 8 per cent cash reserves which we must hold with the Bank of Canada. The \$1½ billion represents our till money—the tools of our trade—to perform our banking functions. There is no relation between these Bank of Canada notes, which you refer to, and the cash reserves of the near-banks which, as Mr. MacIntosh said, are held as a deposit with the chartered banks. There is no relation between the two.

Mr. GRÉGOIRE: But these cash reserves of the trust companies and finance companies are deposited with chartered banks. And are not these cash reserves included in your cash reserves average?

Mr. PATON: They are part of our deposit liabilities, against which we must hold—

Mr. GRÉGOIRE: But if these cash reserves are deposited with the chartered banks, then the chartered banks, having these, can count them as part of their cash reserves, too.

Mr. PATON: No, sir.

Mr. GRÉGOIRE: Why not? They are just cash reserves—

Mr. PATON: They cannot be an asset of one institution without being a liability of the other. As soon as they put them with us then we have a liability to the near-bank. We owe them this money.

Mr. GRÉGOIRE: Yes.

Mr. PATON: That is a deposit liability of ours from which we must allow 8 per cent to be placed with the Bank of Canada.

Mr. GRÉGOIRE: Yes; but suppose a trust company like RoyNat—or a near-bank, like RoyNat—has \$1 million as cash reserves—or let us suppose any figure you want. It is cash. They deposit it with the Royal Bank of Canada. The Royal Bank of Canada owes it to RoyNat, but as long as it remains in the vault of the Royal Bank of Canada, or in their cash—what is the word?—

Mr. PATON: Their till money?

Mr. GRÉGOIRE: Yes.

Mr. PATON: —This is the point I am trying to get across to you, that there is no relationship; the notes are not piled up in the vault—a million dollars worth.

Mr. GRÉGOIRE: I know that; but every two weeks, when you calculate your cash reserves, as you said last week, or the week before, the money that you have in your bank as cash, at the end of the two week period, is included in your average cash reserves.

Mr. PATON: That is correct, sir.

Mr. GRÉGOIRE: So that if you have deposits—

Mr. ADDISON: I would like to raise a point of order. I fail to see the point of Mr. Grégoire's argument in so far as the interest section is concerned. Some of us here are interested in interest.

Mr. GRÉGOIRE: I will arrive at that, Mr. Addison.

Mr. ADDISON: Mr. Grégoire is interested in his theory.

Mr. GRÉGOIRE: I will arrive at that.

The CHAIRMAN: I think that there is merit in the point of order to the extent that although we have to allow members some reasonable latitude in preparing the way for the point he wants to raise, I think that the member in directing his questions to the witness should not try to start at ground zero. In theory you could start with any of the most elementary concepts of banking theory and if the point is not reached fairly quickly then it would be valid for the member to suggest that he could explore from the beginning any aspect of the whole concept of banking and the monetary theory in an attempt to arrive at a certain point.

Since, at this stage, we are not debating the issues amongst us as members of the Committee—we will have an opportunity to do so—I suggest that not only Mr. Grégoire but all members participating in the work of the Committee try to realize that we have a lot of ground to cover as a Committee and to move as quickly as we can to the—

Mr. GRÉGOIRE: Mr. Chairman, perhaps the reason is that we did not have time to clarify the general line of questioning in the beginning.



I will stop at this point and I will come back to it later on when we return to the interest problem.

Mr. ADDISON: Mr. Chairman, on that point of order, we agreed as a Committee that we would take this brief section by section. The Committee agreed to that.

The CHAIRMAN: That is right.

Mr. GRÉGOIRE: Yes.

Mr. ADDISON: Well, I suggest that we stick to what we agreed to.

Mr. GRÉGOIRE: Oh, yes; but I say that this situation arises from the fact in the beginning we did not clarify the general parts we wanted to clarify. We agreed to go with this, but I think we should have clarified the general situations first.

However, I will come back again—

The CHAIRMAN: It may be that other members of the Committee do not share your point of view on how far we got along the road of clarification but they will want to proceed.

Mr. GRÉGOIRE: Perhaps we can come back to it at the end.

Out of \$2½ billion bank notes, \$1½ billion is in cash reserves held by the chartered banks or deposited with the Bank of Canada, and \$1 billion is with the public. Is that correct?

The CHAIRMAN: I will ask Mr. Paton to answer that question and then I will ask Mr. Grégoire to proceed immediately to the point he is getting at and place his question and move on to his next point.

Mr. PATON: The figures as of November 9 are generally around the same figure, Mr. Grégoire. The situation is that as of November 9 the banks held \$473 million Bank of Canada notes and the public held \$2,169,000,000, making a total \$2,642,000,000.

Mr. GRÉGOIRE: What I have here is to October 1966.

Mr. PATON: The corresponding figures in October 1966 are \$468.9 million for the chartered banks and \$2,103,000,000 held by others.

Mr. GRÉGOIRE: Is the Bank of Canada not included among the other depositors in the \$1,055,000,000 deposited in the Bank of Canada as of September 1966?

The CHAIRMAN: I would ask the witness not to answer at this point. We seem to be sticking to the general area of discussion of composition of reserves, and I think if for no other reason than as a courtesy to others participating in the work of the Committee, taking into account the need to have some general preparation for some of the questions that are complicated, I would ask Mr. Grégoire to place his question—

Mr. GRÉGOIRE: What do you want me to do, stop questioning?

The CHAIRMAN: No—

Mr. GRÉGOIRE: No? May I ask for some information first?

The CHAIRMAN: Well, you have been doing that.

Mr. GRÉGOIRE: I am trying to arrive at a certain point and I would like to have some information before I come to the question of interest.

The CHAIRMAN: Why do you not ask your question first and then get the explanation afterwards?

Mr. GRÉGOIRE: I need the information to ask the question.

The CHAIRMAN: May I make a suggestion which you may find useful. Why do you not put certain premises to your question.

Mr. GRÉGOIRE: My premise is this: The effort of the banks to bring in deposits will not be in accordance with the interest they will pay but according to the cash reserves they have.

The CHAIRMAN: I think that is quite a useful question.

Mr. GRÉGOIRE: That is the point I want to reach, but first I want to clarify this question of cash reserves and then I will arrive at this question, which is not the main factor in bringing in deposits.

The CHAIRMAN: No, but it is the main factor in our agenda at this point. Since you have raised a very useful question perhaps we should invite our witnesses to deal with it.

Mr. GRÉGOIRE: I would first like to have some clarification on cash reserves. You say, and I admit this, that there is \$468.9 million held by chartered banks and \$2,103,000,000 held by others. Is it not the fact that "these others" include—This is on page 661 of my book—the \$1,055,000,000 Bank of Canada deposits by the chartered banks? Is that not one of the others?

Mr. PATON: Mr. Grégoire, I am told that this total that you refer to of \$2,572,000,000 on page 658 consists of notes held outside the Bank of Canada.

Mr. GRÉGOIRE: The \$2,100,000,000?

Mr. PATON: The \$2,572,000,000 that you see on your statistical summary there for September 28.

Mr. GRÉGOIRE: So, the notes that you have on deposit with the Bank of Canada are not notes in circulation?

Mr. PATON: We do not have notes. When you say we, the chartered banks do not have Bank of Canada notes on deposit with the Bank of Canada.

Mr. GRÉGOIRE: Then your Bank of Canada deposits are not Bank of Canada notes?

Mr. PATON: No, sir. Our Bank of Canada deposits are deposits to the credit of the individual banks and they, together with this \$468 million worth of Bank of Canada notes that we hold constitute our 8 per cent reserve with the Bank of Canada.

The CHAIRMAN: Now, what was your question about it, sir?

Mr. GRÉGOIRE: I will have to challenge that, Mr. Chairman, because I cannot accept that answer. I will bring the statistics with me tonight. It is too bad that I do not have them with me.

I will come straight to the point. You say you want to increase the deposits and by increasing the interest it will allow you to pay a bigger interest rate to your depositors and that will increase deposits.

Mr. PATON: It will increase our ability to attract deposits.

Mr. GRÉGOIRE: You cannot have more deposits without having more cash reserves. Is that correct? Now, if the Bank of Canada—

Mr. PATON: Excuse me just a moment. As I tried to explain to Mr. Thompson, my reserve is automatically adjusted to my deposit total and therefore the 8 per cent reserve is related to my deposit with the Bank of Canada. We advise them our weekly averages in our return on Wednesday of each week.

Banks invariably keep a surplus over the 8 per cent on the average to take care of the variance in their deposits, and this 8 per cent is a moveable figure, depending on our deposit total. The greater the deposits the greater the 8 per cent. It is not right to say that we have to have the reserve first and then we can get the deposits.

Mr. GRÉGOIRE: Suppose the Bank of Canada does not increase the notes in circulation. They decide not to increase the notes in circulation for six months. You have \$469 million and the public needs \$2,103,000,000 of this. They keep 10 per cent for general operations. Because it is a need of the public you cannot attract this \$2,103,000,000 of Bank of Canada notes. If the public keep it because they need it, you will not be able to increase your \$468 million of Bank of Canada notes. Is that correct? There is only \$500 million and the people keep \$2,100,000,000 and you have \$468 million and if the people need it they keep it, so you will not be able to increase your cash reserve.

Mr. PATON: There is no connection whatsoever, on the basis that you are putting your premise forward, between our deposits and the bank notes that are in circulation and those that you have in your pocket and I have in mine. Perhaps I should not say there is no connection, because it is a contributing part of the money supply of the country, but it is not the basic commodity on which bank deposits are available.

Mr. GRÉGOIRE: I know that. What I mean is that your \$468 million of Bank of Canada notes is calculated in your cash reserves.

Mr. PATON: Correct.

Mr. GRÉGOIRE: If you cannot attract the other \$2 billion, or if the Bank of Canada does not issue any more Bank of Canada notes, you will not increase your cash reserves.

Mr. PATON: But the Bank of Canada can still, even if they did not issue any other paper money, increase or decrease the money supply. It is from that money supply total that we attract deposits.

Mr. GRÉGOIRE: Suppose they do not increase the money supply—

Mr. PATON: You were on Bank of Canada notes a few minutes ago and now you are on money supply.

Mr. GRÉGOIRE: What do you mean by money supply? How do you translate that in French?

(French)

M. PATON: La masse monétaire.

(English)

Mr. GRÉGOIRE: Yes, but the Bank of Canada deals only with 8 per cent of the money supply, not with the other 92 per cent.

Mr. PATON: I wonder how Mr. MacIntosh is feeling?



The CHAIRMAN: I will let Mr. MacIntosh make a comment and then we will pass on to Mr. Latulippe, because Mr. Grégoire's 20 minutes has more than gone by.

Mr. GRÉGOIRE: After Mr. Latulippe has finished and there is more time, I will come back for another round.

The CHAIRMAN: Could you make any comments which would clarify this very interesting point?

Mr. GRÉGOIRE: Let us start again.

*(Translation)*

Mr. LATULIPPE: Thank you very much, Mr. Chairman. My questions are still pretty elementary but they will be pretty short too. Could you tell us if, when banks make loans, they lend money coming from other people? When banks make loans, do you lend other people's money?

*(English)*

Mr. MACINTOSH: Mr. Latulippe, when we make loans we borrow money from the public. So, in a sense, since we have borrowed the money, it is our money but we have a debt to the public. When we make loans I suppose in a sense you could say we are lending other peoples' money, but only in the sense that we have a debt to them.

*(Translation)*

Mr. LATULIPPE: Mr. Chairman, if this is the case and if the bank does lend other people's money, this necessarily creates a new deposit, is that a fact?

The CHAIRMAN: Mr. Latulippe, have you related your questions to the item on interest rate?

Mr. LATULIPPE: Yes.

The CHAIRMAN: Because the Committee decided a few days ago that our questions should be limited to that particular point.

Mr. LATULIPPE: Yes, but I am preparing the ground for my questions too, my questions will not exclusively be on interest rate, but they do have a close connection with them.

The CHAIRMAN: Go ahead, but I did intend putting a suggestion forward, I think it might be better to proceed in a straight line rather than go about this in such a circuitous manner.

Mr. LATULIPPE: Still I put several questions on interest rate last time. These questions relate to general bank economics, and I will return to the actual matter of interest rate eventually. So, if you lend other people's money, this creates a new deposit. Every time you lend money, it creates a new deposit?

The CHAIRMAN: I might be wrong, but I do feel that we have spent sufficient time on this question of money supply, creation of money, creation of deposits, and so on, I believe it would be the Committee's intention to discuss such problems as are related with Government proposals in respect of interest rates: are these good proposals, are these bad proposals and so on. I would suggest that we cannot go over the whole ground again. I think we should begin by putting more restricted questions.

Mr. LATULIPPE: But the questions we are putting relate to the interest rate, as has been the case for all questions put so far.

The CHAIRMAN: But when we will have concluded our questions on the bankers' brief, we will have an opportunity to return to these more general matters, but I think we should seek to discipline ourselves to some extent, I think we should try to restrict our questions, otherwise we will never get to the end of all this.

Mr. LATULIPPE: Since my questions do not specifically deal with interest rates, I will return to this when a further opportunity is offered and when the Committee is ready to entertain more general questions. I am therefore satisfied to let other people put questions as long, of course, as we are dealing with interest rates.

(English)

The CHAIRMAN: I have no further names on my list at this point and that being the case I suggest—

Mr. THOMPSON: Mr. Chairman, I wonder if I could ask for information purposes only a single question that relates to an answer given to a previous question which was based on the proposition I put forward a little while ago. I stated that probably more important to the banks than an increase in interest rates was the decrease in the reserve ratio. You mentioned, Mr. Paton, that you immediately deposit with your reserve funds 8 per cent of your deposit liabilities. Is it not true that your reserves are made up of Bank of Canada notes and Bank of Canada deposits?

Mr. PATON: Bank of Canada notes and deposits with the Bank of Canada, that is correct.

Mr. THOMPSON: Yes, with the Bank of Canada. Now, that being true, can you elaborate on the answer you gave to me that immediately a deposit liability is made that under the present legislation you deposit 8 per cent of that into your reserve account, when probably that deposit liability was not made with Bank of Canada notes or Bank of Canada instruments at all.

Mr. PATON: Mr. Thompson, each bank's account with the Bank of Canada has a number of daily entries in it. That is the account through which we settle all our clearing balances, be they debit or credit, right across the country in all of the Bank of Canada points. We provide the Bank of Canada with statistics on a weekly averaging basis and at the end of each month we know the 8 per cent average total deposits and Bank of Canada notes that we must carry with the Bank of Canada for the ensuing month. This is the *modus operandi* of the arrangement we have with the Bank of Canada. While in theory exactly what I say takes place, it is enveloped in entries every day covering our operations right across the country. We have a fixed amount that we operate on for each month which is taken from the previous month's averaging periods.

Mr. THOMPSON: Thank you, Mr. Chairman.

Mr. FULTON: If you have exhausted the interest question and want to get on to some of these other ones which really are causing some indigestion—

The CHAIRMAN: I think there are some topics that can never be exhausted completely. Since at this point we have no—

Mr. CLERMONT: Mr. Chairman, before you go into another subject, I understand that Mr. Nicks, or somebody else from the Bankers' Association, may have a reply to a question I asked last week regarding differences in consumer interest and discount loans. I also understand we are supposed to sit here tonight at 8 o'clock, but there might be a vote at 8.15 in the House of Commons.

The CHAIRMAN: That is right. I think Mr. Clermont has raised a useful procedural point. I will keep that in mind. No one is expected to rush here at 8.00 p.m. and rush out again, but since I was not presiding this morning I will have to rely on the Committee. Has this question that you asked been dealt with as yet?

Mr. LAFHAMME: It has been suggested that we could resume our sitting at 9 p.m. if the vote took place at 8.30 p.m.

The CHAIRMAN: It is true that as a practical matter it would take about 15 minutes for the members to walk over here to resume, so we agree that our evening session will begin at 9.00 p.m., and I thank you for raising that point.

Mr. Clermont has another point to which I was referring about—

Mr. CLERMONT: It was last week, when the Bankers' Association brought before this Committee a schedule of eight sheets concerning interest and discount and service charges on consumer loans. I understand they are now ready to explain or give more information on some of the differences.

The CHAIRMAN: These are the differences in the amounts charged on the basic types of loans? Is that correct?

Mr. CLERMONT: Yes.

The CHAIRMAN: I know that people like Mr. Fulton have been waiting very patiently to deal with some of the other questions.

Mr. Dixon?

Mr. DIXON: Mr. Chairman, as I recall the question raised last week related to the differing amounts on these eight schedules for the interest or discount on a personal loan of \$1,000 repayable in various installments. It is the case that there is more than one interest table. They have been using computers and other means over the years, and there is more than one interest table for 6 per cent, depending on how many decimal places they have taken the calculations to, so when I used the word "rounding", or a different table, last week this accounts for the minor differences between the interest charged by each bank.

It is the case also that for banks "B", "E" and "F" the interest charges, I believe—at least in the case of \$1,000 for 12 months are exactly the same, namely, \$32.50. In the case of bank "A" and bank "G", I am given to understand that the bank makes a loan of \$1,000, and to the loan of \$1,000 they make an additional loan in the amount in each case of a service charge of \$19.35. Then they compute interest at 6 per cent per annum on the reducing principal amount of \$1,019.35. Therefore the annual interest on that is \$33.13 in one case and I think it is \$33.12 in the other. So the difference, therefore, between the basic \$32.50 and the \$33.13 is the interest on the service charge which has been added to the loan.

The CHAIRMAN: What if the prospective borrower in the case of the second loan insists on paying the service charge out of his own pocket on the spot?



Mr. DIXON: I presume that bank will then accept it and will charge \$32.50.

The CHAIRMAN: Who are they? What is the initial?

Mr. DIXON: "A" and "G".

The CHAIRMAN: We have the names now. The Bank of Montreal and the Banque Canadienne Nationale. Perhaps representatives of these banks could inform me whether they would refuse to give a prospective borrower a loan if he came in and wanted to pay the service charge out of funds he already had in his pocket?

Mr. DIXON: No, I am quite sure that they would not refuse to give him the loan but, rather, they would be charging interest on the amount of money which he got, in that case \$1,000.

The CHAIRMAN: They would not insist on his borrowing the service charge?

Mr. DIXON: No. Please appreciate that there is a system in an organization and a great volume of these loans are made. I say again that this is left up to the customer, but here each one of these banks has this system and I am sure that in 99 per cent—

The CHAIRMAN: This is a way the consumer could save a little money for himself.

Mr. DIXON: Possibly. Now there was another part to the question, Mr. Chairman. In the case of bank "E" I believe basically the question was why was there such a great difference between the interest or discount shown in the case of bank "E" compared to all of the other banks.

Mr. CLERMONT: No, bank "E" did not show any division between the interest and the service charge.

Mr. DIXON: Yes. As I say, there is no division there because this bank, in the accounting system which it uses for its personal loans, treats the \$1,000 loan for 12 months as though the \$1,000 loan is outstanding for one year, and they discount that loan at 6 per cent. Now then, coincidentally with discounting the loan of \$1,000 for one year at 6 per cent, they make an agreement with the borrower to place 12 equal deposits in a savings account in an amount which, at the end of 12 months, will equal the \$1,000 loan. They also give interest on those accumulating deposits, and that is also credited to the borrower.

Therefore, they do not use any service charge, but they use what has been called in the United States—and I understand this was discussed at great length on previous revisions—the Morris Plan System and, as you can see, the net discount cost to the borrower in the case of bank "E" is close enough to the combined interest and service charge cost of the other banks.

Mr. CLERMONT: But for 36 months there is still a difference because they are, I think, the second highest. For 36 months the total is \$174.85 and there is one at \$162.

Mr. DIXON: I can only suggest that the difference that shows up on the 36 months is due to the compounding factor of discounts.

The CHAIRMAN: Perhaps now that the names of the banks in question are a matter of public information we will be able to have a practical experiment in the operation of the forces of competition.

Mr. DIXON: We have been having that now for some time.

The CHAIRMAN: But the information is put together in a handy document.

Mr. DIXON: It has been put together for this Committee.

The CHAIRMAN: It is also for the public. This is a matter of public record.

Mr. FULTON: If the public can wade through the extraordinary jumble of evidence, Mr. Chairman, the way it has been tossed back and forth.

The CHAIRMAN: Our gatherings are also being covered by the press, and who knows, some ambitious young writer might want to draw all this information together into one article, which will be put out across the country through the various media. Who knows?

Mr. LIND: With regard to this \$1,000 loan, when do you take the income into your account, at the start of the loan or the finish of the loan?

Mr. DIXON: When a person borrows \$1,000 and signs a note, as in the case of bank "A" for \$1,052.48, the total amount of income to the bank is usually put in what I will call a suspense account and is taken in on a pro rata basis, that is, a twelfth the first month and another twelfth the second, third, and so on, throughout the life of the loan.

Mr. LIND: You give the borrower the whole \$1,000 though, do you?

Mr. DIXON: That is right.

Mr. LIND: You came up with a new term to me, "rounding" out the interest, that I had not heard before. Do the banks do any rolling of their paper?

Mr. DIXON: I would like you to define for me, sir, what "rolling" of paper is.

Mr. LIND: Do you age your accounts receivable?

Mr. DIXON: No.

Mr. LIND: I understand that finance companies rewrite the term of the loan. If a person gets in trouble and cannot pay on a 12 month term they change it to a 24 month term.

Mr. DIXON: I now know what you mean by your reference to "rolling". I think in the banks' offering of total service to the borrowers it is the case that loans are extended when borrowers are unable to meet the payments that have been originally set. It is sometimes more convenient and, indeed, more suitable to him to refinance and extend the term to something that is more suited to his budget. But again there are limitations to this, usually because of the length of time for which his income is assured, or the security which has been offered, as in the case of an automobile, is depreciating rapidly. Consequently such refinancing or re-extending of the term is done on a very careful basis and worked out with the borrower.

Mr. LIND: Do you extend your term any longer than 3 years?

Mr. DIXON: I believe in some cases the banks are making personal loans for longer than 36 months.

Mr. LIND: What is the largest personal loan that the banks will make? Is it \$5,000 or \$10,000?

Mr. DIXON: Those would be the exceptions rather than the rule. After all, they are based generally on the borrower's ability to repay, and because he

usually earns his income on a monthly basis we measure his ability to repay on a monthly basis. Therefore, having in mind the purpose of the loan, the kind of security and the borrowers ability to repay, this is what generally governs the repayment terms.

Mr. LIND: If the loan is for some type of building repair, is it without recourse or is it with recourse?

Mr. DIXON: I think that would be up to the individual bank, but I think it is fair to say that most of the personal loans of most of the banks are without recourse.

The CHAIRMAN: I am also reminded that Mr. Gilbert requested that the various forms that the banks ask their customers to sign with respect to keeping an account involving authorization for various charges, and so on, be tabled for the inspection of the Committee, and Mr. Paton informs me that these documents are available. I think it would be useful if we disposed of this item and have this material taken care of.

Mr. CLERMONT: This was requested by me, sir.

Mr. PATON: I beg your pardon, I am at fault.

Mr. DIXON: It was my fault.

The CHAIRMAN: This just shows the co-operative, non-partisan spirit of enquiry that we are developing in this Committee.

I would suggest that perhaps the best thing to do would be to have these parcelled out, and perhaps the clerk can have them taken around to the offices before supper. Or would some people like to carry them away with them?

Because we have a certain freedom of choice here we will let each member decide whether they want to carry away their own bundles of forms or have them delivered to their office. You cannot say that we are not cooperative here.

It would appear—and I am subject to correction on this—that we have finished the—

Mr. GRÉGOIRE: I have a question to ask on interest.

The CHAIRMAN: You have a question you want to ask right now on interest? All right, this is the only name I have, and that being the case I will recognize Mr. Grégoire. In the meantime we can continue with the distribution of the documents.

*(Translation)*

Mr. GRÉGOIRE: This morning, in concluding my questioning, we were on Clause 91 of Bill C-22 and of the possible elimination of the interest ceiling. Should the yield on short-term government bonds come down to  $4\frac{1}{2}$  percent for a three-month period, this will bring about a removal of the ceiling. I was told that this would be of general advantage to the banks, since, from that level on there will be no further limitation on interest ceilings. From that point, therefore, I would like to move to something else. What is the total amount of short-term government bonds on the market at the present time?

*(English)*

Mr. MACINTOSH: It is approximately \$3.5 billion, Mr. Grégoire. I have not made an accurate calculation of it, but it can be determined from the Bank of Canada statistical summary. I think \$3.5 billion is close enough.



(Translation)

Mr. GRÉGOIRE: On that amount, what is the amount of short-term bonds held by chartered banks generally?

(English)

Mr. MACINTOSH: That, too, you can find in the Bank of Canada statistical summary in the bottom table on page 661, four columns in, \$817 million at August 1966.

(Translation)

Mr. GRÉGOIRE: Now, Mr. Chairman, short-term bonds are bonds at three years or less?

(English)

Mr. MACINTOSH: Yes, I should correct myself there. The figure which I gave you, \$3.5 billion, consists of the amount of under two years altogether, plus a rough estimate I made of the amount which is due between two and three years, so there would be about \$3.5 billion. Now, if you were to include the holdings of the banks between two and three years to maturity I would expect there would be another \$300 million or \$400 million. There would be, perhaps, \$1,200,000,000 altogether.

(Translation)

Mr. GRÉGOIRE: This indicates that one-third of short-term Government of Canada bonds is held by chartered banks?

(English)

Mr. MACINTOSH: Yes, sir.

(Translation)

Mr. GRÉGOIRE: One third, then, of short-term Government of Canada bonds is being held by chartered banks at the present time?

(English)

Mr. MACINTOSH: Yes, sir.

(Translation)

Mr. GRÉGOIRE: Since we are dealing here with a three-month period, concluded on January 1 or on July 1, the interest rate has to come down to  $4\frac{1}{2}$  percent for the limitation to disappear. Now, if there are twelve three-month periods over a three-year period, can we say that government bonds have an average equal yield over a three-month period? Are there higher yields during some periods and lower yields during some others? Can it be said, for instance, that on the average, every three months the government issues for \$300 million in short-term bonds, which would be \$3,500 million in three years, or thereabouts.

(English)

Mr. MACINTOSH: Well, Mr. Grégoire, the government issues bonds from time to time at interest rates that are determined by market conditions at that time. It is not a question of them issuing a fixed amount every three months, it depends upon the structure of the debt. Even if interest rates were to change abruptly for new issues for a period of three months, the rest of the debt would be affected.

You cannot affect one part of the debt alone. There is only one total debt. They are all related to each other. If you affect the interest rate on one issue, you affect it on all issues.

Mr. FULTON: Does that not take effect by changing the market price of the bond? If you just left your answer where it lay, might we not infer that there was a change in the interest rate attached to the bond, whereas in fact the effect is to change the market price of the initial yield of the bond?

Mr. MACINTOSH: Yes, Mr. Fulton. Perhaps I did not make that clear. Market prices change and yields fluctuate accordingly, but the coupon rate which was originally fixed on the bond remains unchanged.

(Translation)

Mr. GRÉGOIRE: Now, Mr. Chairman, the actual yield of these short-term bonds is not the same as the medium or long-term bond yield? Is that a fact?

(English)

Mr. MACINTOSH: Yes.

(Translation)

Mr. GRÉGOIRE: The interest on 20 year bonds is higher than the interest accruing over a two-year term?

(English)

Mr. MACINTOSH: Yes, usually. It is not always the case. There have been cases within the last ten years when treasury bills went actually somewhat higher than long term bonds.

(Translation)

Mr. GRÉGOIRE: But generally, short term loans yield less than long term loans, and the interest yield on short term bonds, not being the same as the long term yield is determined according to demand. If there is a high demand for long term loans or bonds, then there will be a tendency to lower the interest rate. If there is a lower demand the interest rate will be higher.

(English)

Mr. MACINTOSH: This is true, yes, of both short and long term bonds. It is true of all bonds.

(Translation)

Mr. GRÉGOIRE: If there is a high demand for short term bonds, the interest rates will be lowered?

(English)

Mr. MACINTOSH: Yes.

(Translation)

Mr. GRÉGOIRE: If there is little demand they will go up?

(English)

Mr. MACINTOSH: That is correct. Other things being equal. You always have to say other things being equal. They are not always—

(Translation)

Mr. GRÉGOIRE: But it is not the same interest rate in all cases. Long term bonds or short term bonds?

(English)

Mr. MACINTOSH: I can visualize a situation where the demand for short term bonds is going up, and the supply is going up equally, and interest rates will not change. So you cannot say as the demand for short term bonds goes up their prices will go up and the yields will fall, because if the supply goes up equally the price will remain unchanged. If the demand for potatoes goes up and the supply goes up equally, the price of potatoes will not change. It is the same thing.

(Translation)

Mr. GRÉGOIRE: You mentioned this morning that you did not feel that the average yield of short term loans would go down to  $4\frac{1}{2}$  per cent. You mentioned as much this morning. You said that this would be a condition which would not vary in the near future. Is there any advantage then, for this yield to be higher so as to have a larger margin. That is what we were discussing this morning. If the chartered banks hold  $\frac{1}{3}$  of the short term bonds, would not this bring about an increase in the interest yield on short term bonds?

(English)

Mr. MACINTOSH: Mr. Chairman, I would like to clarify one point here. If there is an assumption that the banks can manipulate the level of interest rates, I would like to deny that right away. Perhaps this point was not clear the other evening when we concluded, but it is entirely and absolutely beyond the capacity of the banks to manipulate interest rates for their own purposes.

Mr. GRÉGOIRE: I have not said that yet.

(Translation)

But you did admit that if the public demand for short term bonds is high, the interest rate will go down. If it is weak and if the public does not take out short term bonds, the interest rate will go up, since the Government will be looking for buyers. You admitted as much—where the weak demand of the interest rate goes up, with a high demand the interest rate goes down?

(English)

Mr. MACINTOSH: Other things being equal, I admit that.

Mr. CAMERON: Could I suggest, Mr. MacIntosh, that the difference between an interest rate and an effective yield be made clear.

Mr. MACINTOSH: An effective yield?

Mr. CAMERON: Yes, I think this is where some of the confusion arises.

Mr. GRÉGOIRE: Yes, I am speaking about the return of yield.

Mr. MACINTOSH: I think this was the point that Mr. Fulton was making earlier, that the interest rate on a 4 per cent bond issued two years ago to the original buyer who bought it at par yield 4 per cent may only trade on the market at 96 or 98 now, in which case the yield on it in the market may be 6 per cent but the interest coupon will be 4 per cent. It all depends on the price of the bond.



(Translation)

Mr. GRÉGOIRE: I am speaking of the yield here, I am speaking of the yields from the beginning. If the demand is weak, the yield would be higher for the buyers. Since chartered banks constitute  $\frac{1}{3}$  of the market for short term bonds, if banks cease to buy the demand will be reduced by 33 per cent. Will this increase the yield?

(English)

Mr. MACINTOSH: I think I see where you are heading, Mr. Grégoire, and keeping that in mind I would say yes. If we withdrew from the market the yield on short term bonds would go up. You want me to add the contrary point, I think, that if we buy more the yield would go down. Subject to our capacity to buy, that would be true.

(Translation)

Mr. GRÉGOIRE: So if you anticipate that the yield will not go down to  $4\frac{1}{2}$  over the short run, the advantage of the banks is to see that the average yield of short term loans increase as much as possible, because at that point, if the average yield of short term bonds rises to 6 per cent, it will allow you to lend at  $7\frac{3}{4}$  per cent.

(English)

Mr. MACINTOSH: Once this Bank Act is in effect a higher level of yield on short term bonds would shift up the ceiling. It would not necessarily shift up the average we charge, nor would it necessarily shift up our margin, because our costs of deposits would also go up. This is a two-sided problem.

(Translation)

Mr. GRÉGOIRE: But it will increase your possible maximum ceiling? So, there is every advantage for you to increase your ceiling—I am not speaking of the actual rates—is there not?

(English)

Mr. MACINTOSH: You have reversed the field since this morning, because I understood you to say then that it was to our advantage to lower the interest rates on bonds in order to remove the ceiling. Our view has never been that it is to the advantage of the banks one way or the other from the point of view of the over-all level of rates. Our view is that it is to the general public interest to have the ceiling removed so that we can behave more flexibly in the market, that is all.

The CHAIRMAN: What would happen if the chartered banks stayed out of this bond market?

Mr. GRÉGOIRE: The short-term bond market?

Mr. MACINTOSH: The short term market. I think the Minister of Finance would be very concerned because the chartered banks are a very important part of the short term bond market. Mr. Chairman, the banks cannot be out of that market because this is where a major part of their short term liquidity rests. They must be there. Not being in that market amounts to being in the condition of some institutions that we know of.

The CHAIRMAN: You are not referring to banks?

Mr. MACINTOSH: Not to chartered banks.

Mr. LAFLAMME: Do you mean that you do not like to buy those bonds but you have to do it?

Mr. MACINTOSH: In a general way I suppose that is true, Mr. Laflamme. The banks hold bonds for liquidity reasons, not really for reasons of earnings.

*(Translation)*

Mr. GRÉGOIRE: But could you find such short term loans elsewhere than in Government bonds? Let us assume that you want to force the Government to increase the average yield of the short term bonds, and if you decided to withdraw from that market, and if you bought the short term bonds from provincial governments, you would have the same advantage in respect of short term liquidity, and it would force the Government to increase its yield. In other words, Mr. Chairman, by providing for this transition period, is not the Government suspending a sword of Damocles over its own head. Is not the Government obliging the banks to force it, that is to force the Government to increase the yield? Is not the Government putting itself in a difficult position? If the banks want to increase their interest rates, they will have to force the Government to increase the yield. Is that not the position in which the Government is going to put itself?

The CHAIRMAN: I will allow Mr. MacIntosh to answer, but I believe you should put that question to the Minister of Finance who will appear before us. I will allow Mr. MacIntosh and his colleagues to give their views on that matter, I do not know whether this is a realistic view of the position.

Mr. GRÉGOIRE: Could I put another question? Since Mr. MacIntosh is an economist, the businessmen here who deal with the actual workings of the banks, are the General Managers.

*(English)*

Mr. MACINTOSH: Mr. Grégoire, I object to that. I deal with our investments. This is my function in the bank. I am not primarily an economist.

*(Translation)*

Mr. GRÉGOIRE: But the people who deal with investments and so on are the General Managers of banks.

The CHAIRMAN: But when Mr. MacIntosh speaks, he speaks on behalf of the Bankers' Association, and if his colleagues allow him to answer, I think it is not up to us to say that he should not. He is expressing the views of the Association.

*(English)*

Mr. MACINTOSH: If I may repeat, I am not a research economist. I am not an economist at all in the bank at this stage. In fact I am in charge of our investment operations, and I hope in that sense it is practical.

It seems to me, if I may make a short answer, Mr. Chairman, that if the implication is that we could organize some sort of conspiracy to either force the ceiling off by pushing yields on Government of Canada bonds down, or force their rates up by withdrawing from the market and shifting to other types of securities, that this is so improbable that I would not want to give it credence by even suggesting that it is a possibility. It is quite out of the question. The banks

hold part of their liquid assets in Government of Canada securities, and we could not find this liquidity in any other form of short term security. Even if we could, we would not organize that sort of a game against the Government of Canada. Even if we did, as I said this morning, the Minister of Finance could soon defeat it by issuing all the bonds that we wanted. He could issue them as fast as we bought them. That was by point.

(Translation)

The CHAIRMAN: I would like to ask the Vice-Chairman whether these questions have all been covered this morning.

Mr. LAFLAMME: Yes, a number of questions were put on that point this morning.

Mr. GRÉGOIRE: Not on that specific question.

Mr. LAFLAMME: I cannot remember whether specific questions have been put on that point, but the general question was well covered this morning.

The CHAIRMAN: I will allow Mr. Grégoire to put one or two questions more, because his time is almost up.

Mr. GRÉGOIRE: Mr. MacIntosh you say you have no intention of doing so, however, once the Act has been carried since the chartered banks do not wish to have this transition period, is it possible for them to put the Federal Government in a difficult position because of their wish to increase the average yield of short term bonds?

(English)

Mr. MACINTOSH: The answer is definitely not.

(Translation)

Mr. GRÉGOIRE: You could not withdraw from a short term bond market to move into provincial short term bonds instead?

(English)

Mr. MACINTOSH: It seems to me that you are forgetting, Mr. Grégoire, that the Bank of Canada is in a position to offset any operations we carry out which affect our cash reserves. We are not free to just go as we please and sell off one asset and acquire another. The Central Bank is in a position to advise the Minister of Finance, for one thing, to issue 25 billion bonds if we want them so much. What would we do for money?

(Translation)

The CHAIRMAN: Before we move into this very interesting measure, which is not however within the rules, I want to say Mr. Grégoire's questioning time has expired.

Mr. GRÉGOIRE: Mr. Chairman, does this automatically shut off all questions on that matter? Are we moving to another subject?

The CHAIRMAN: Yes.

Mr. GRÉGOIRE: If nobody else wants to put questions on interest rates, I cannot continue to put questions.

The CHAIRMAN: Quite so.



Mr. GRÉGOIRE: Oh, no. I have not been running around in circles. I find this transition period difficult for the Government itself.

Mr. LAMBERT: But we have the Bank of Canada.

(English)

The CHAIRMAN: I would now ask the Committee to turn their attention for the time being to the next section.

Mr. LIND: Could the banks not increase the amount of money supply at the present time if they wished to decrease their holdings of bonds?

Mr. PATON: No, sir, Mr. Lind, they could not affect the money supply. All they would be doing would be changing the mix of their assets, and only good business operation would dictate whether they should or not.

Mr. LIND: I realize that, but is there not a margin of flexibility there that they could come a little closer to 13 per cent? They have an 8 per cent reserve and 7 per cent in short term Government bonds.

Mr. PATON: No, sir, the 7 per cent secondary reserve you are referring to is solely comprised of treasury bills, and day to day loans not Government bonds. The day-to-day loans to investment dealers are against the security of treasury bills, and the latter cover 90 or 180 day maximum term. They have nothing to do with the short term Government bonds. Even if a Government bond is within 6 months of maturity, it does not come into that 15 per cent area to which you refer.

(Translation)

Mr. GRÉGOIRE: I would have a few questions to put on the interest rate as dealt with in the brief.

The CHAIRMAN: I regret but the Committee was in agreement on the suggestion put forward by our Steering Committee. It was decided to have a question period on each matter brought up in the brief submitted by the Bankers' Association. It was also agreed that some other questions could be put to clear up matters which would have been left unclear up to then.

Mr. GRÉGOIRE: But I wanted to deal with interest rates.

The CHAIRMAN: Yes, but it had also been agreed to limit every member to twenty minutes. If I were to adhere to your request at this point you would have a longer question period than others, and others would have a good reason to complain.

Mr. GRÉGOIRE: But I had other questions to put.

The CHAIRMAN: Perhaps you could keep your questions for the general question period which will follow on our discussion of the points within this brief.

(English)

I suggest therefore that the Committee now turn their attention to the issue of mortgage lending. We have had some general discussion on this.

(Translation)

Mr. CLERMONT: Mr. Grégoire has just made a remark. He says it is the first time he has seen the guillotine applied. Mr. Grégoire said that he was not putting

the same questions over and over again. He put the same questions this afternoon, this morning and last week. He has been complaining of the guillotine, but I must say he has had every opportunity to put questions.

Mr. GRÉGOIRE: If my honourable friend wants to read the minutes, he will see that these are not the same questions.

Mr. CLERMONT: I was here.

The CHAIRMAN: It is not the time or place to enter a discussion of this kind. The minutes will show everybody how many occasions were given to honourable members to put their questions. We will have further opportunities later to return to the points raised by the Bankers' submission.

(English)

I would now ask those members who wish to ask questions on the general issue of mortgage lending to signify in the usual manner. If not, I will pass on to the next topic. Mr. Fulton.

Mr. FULTON: In your submission Mr. Paton, you say at the bottom of page 6:

As long as the current pressure of demands on real production capacity persists, the Bank of Canada could be expected to keep a tight rein on the total funds at the banks' disposal. In such circumstances it would not be helpful to anyone to build up unwarranted expectations as to the volume of new mortgage funds that can be provided in the relatively near term.

Without being facetious, if I may say so that seems to me to be a typical bankers' statement. However, it is a fact, I think, and I would ask for the purpose of this discussion that you accept it, that not only do private individuals in either the home building or home buying field, but also people in government have very considerable expectations that the liberty given to the banks to lend on security of mortgage or real property will result in an appreciable inflow of funds into the mortgage field.

You are, as I understand the bill, to be allowed to lend up to 3 per cent in the first year, is it not? I should look up the section, I suppose.

An hon. MEMBER: Clause 76, page 53.

Mr. PATON: You are speaking of residential mortgages, NHA mortgages?

Mr. FULTON: No, conventional and NHA.

Mr. PATON: With conventional mortgages there is no limitation on the banks' participation—I am sorry, I wish to reverse that. On the NHA mortgages there is no limitation. On conventional mortgages there is a limitation. Am I right, Mr. Elderkin?

Mr. ELDERKIN: That is right.

Mr. FULTON: Is the limitation of 3 per cent on the conventional the total mortgages?

Mr. PATON: Ten per cent of our deposit liabilities is the eventual total, but it is only on the residential mortgages that this limitation is imposed.

Mr. FULTON: This section is long and complicated.

Mr. PATON: It is the bottom of page 52. There was an amendment to that, but it was an amendment in wording only and not in substance.

Mr. FULTON: But the banks can only reach that 10 per cent in stages, can they not?

Mr. PATON: It is 3 per cent the first year and 1 per cent a year after that.

Mr. FULTON: Could you then give us an estimate of how close to that permissible maximum you would expect to come?

Mr. PATON: I think that would be difficult, Mr. Fulton, bearing in mind that there are several types of mortgage lending areas we will be going into. For example, if one endeavoured to put a percentage on conventional mortgages one would also have to combine that with the percentage that we would be able to put into NHA mortgages. At present there is a spread. The NHA mortgage rates are  $6\frac{3}{4}$  per cent and conventional mortgages are commanding rates of interest in Toronto of possibly upwards of 8 per cent. I think this would be an area in which each individual bank would be making its own decision. With respect to the investment in these areas, one must also bear in mind that we are looking to these sections to permit us perhaps to be of greater help to our business accounts by virtue of our ability to take mortgages on their fixed assets.

Mr. FULTON: I have been given figures that indicate that for 1966, as compared to 1965, there has been a total reduction of institutional participation—as distinct from mortgage lending by CMHC directly—in mortgage lending of \$853,400,000. Would you care to hazard a guess as to the proportion of that which it might be reasonable to expect the banks to fill? Would it be a half, a third, or, say, \$850 million dollars in round figures?

Mr. PATON: Our total outstanding under NHA mortgages, for example, at the present time is roughly \$800 million, and that is roughly 4.4 per cent on our figures here of our total Canadian deposits.

I would indeed hesitate to put a figure on the participation that we conceivably might be able to take in this mortgage area. I would hopefully think that it would be a reasonable share of the amount that you are referring to, but whether that would be \$200 million or \$300 million, I would hesitate to estimate. Certainly I am conscious of the need and we would be very anxious to get back into the mortgage lending field because many of us have substantial builder connections, and if we can provide them with the mortgage funds concurrently we are aiding their business operations, there is a definite attraction for getting into this lending area on that basis only, apart from a straight involvement in mortgage lending. So I think we could make—shall I say—a constructive impact in this field, subject to the limitations we have stated that as ostensibly we are coming into this new area at a time when other loan demands are so substantially heavy.

Mr. FULTON: Yes, but at the present time it appears you will be subject to an interest ceiling in the neighbourhood of  $7\frac{1}{4}$  per cent on your ordinary lending. Mortgage rates are now running  $7\frac{1}{2}$  to 8 per cent. I am not talking about CMHC mortgages, but conventional mortgages. I realize that the administrative costs in connection with mortgage lending are higher than with your normal lending activity, but would the premium of mortgage interest over your ordinary lending interest, as it appears it will be for a time be a factor in attracting into the mortgage lending field?



Mr. PATON: Yes it would be.

Mr. FULTON: Since it appears that you do not anticipate that you will be into it to the extent to meet the full demands, and since—in my submission at any rate—one of the imbalances in the present National Housing Act situation is that smaller communities, and I do not necessarily mean villages, I mean substantial but still smaller communities, are not served by the trust and loan companies—the normal institution lenders in the mortgage field—because their available money is all snapped up readily in these great metropolitan areas.

On the other hand, the banks usually have at least one branch and sometimes more than one in the smaller communities. In other words, almost every community is served by a bank. Do you anticipate having, therefore, any policy of directing definite a proportion of your mortgage lending activities towards the branches serving the smaller communities? I would hate to see the banks, because it is easier and you can make larger loans in the bigger communities, make them all there and let the smaller communities continue to starve.

Mr. PATON: No I can assure you that our involvement in this area would be spread throughout our entire branch operation, as it was in fact when we entered NHA mortgages back in 1955. One of the basic advantages to this permissive feature in the act is that our managers right across the country would be in a position to present applications for residential mortgages in the areas in which they are located. I think we make this point in our brief, that one of the basic advantages is that we are in many areas where perhaps the usual lenders are not located.

Mr. FULTON: But I am thinking of when there is a squeeze on your available funds, as there is on funds generally, can we anticipate that as a matter of policy the banks may see to it that perhaps a slightly more than strictly proportionate amount of the mortgage funds available would be at the disposal of the branch managers in smaller communities?

Mr. PATON: Yes, I think I can assure you that would be the case. It is similar to our approach to the present day tight money situation where we have been looking after the small businessman to the best of our ability, and perhaps leaning—as you suggest—a little over in their favour. This would also apply to our mortgage lending plans.

Mr. FULTON: This is all I have for the time being.

The CHAIRMAN: I recognize Mr. Johnston followed by Mr. Lambert.

Mr. JOHNSTON: The question I wish to ask was partially asked by Mr. Fulton, I believe. If the interest level remains as it is, what effect would your entry into the mortgage field have on loans to business and industry? Would it reduce the possibility—

Mr. PATON: I am not quite clear on your question, Mr. Johnston.

Mr. JOHNSTON: I assume you tend to argue on the basis that if there is no increase in the money supply you are going to obtain your funds from other institutions, in the sense that you will attract them from other places, so if you go into the mortgage field will this be at the expense of loans to business and industry? Will there be less money available?

Mr. PATON: No sir, it will not be at the expense of any part of our present lending.

Mr. JOHNSTON: In other words, one could foresee a situation where even though the act was changed to allow you to go into the mortgage field, you would in a sense not be in that field because there would be no money directed in that way?

Mr. PATON: Well, of course, I would remind you that we are hopeful that we will attract additional funds to enable us to get into these fields, not only through deposits but also by virtue of the fact that our ability to issue debentures is also included in this act.

Mr. JOHNSTON: Now, would the proposed increase in cash reserves to 12 per cent for short term loans have the effect of again reducing the supply for short term loans if you go into the mortgage field at a higher percentage of interest?

Mr. PATON: The 12 per cent you referred to is the cash reserve against demand deposits. That is offset by the reduction to 4 per cent on term deposits with a net average, as we discussed, of around 6.6 per cent. You have to also consider, assuming constancy in the money supply, that this releases additional funds for lending. However, the 12 per cent ratio has no direct connection with our lending ability.

Mr. JOHNSTON: Thank you.

The CHAIRMAN: Mr. Lambert followed by Mr. Cameron and then Mr. Gilbert.

Mr. LAMBERT: Well, in the field of the conventional residential mortgage loan there has been an indication of a decline in the volume of funds available from the conventional mortgage institutions, and I would think that the bulk of them come from major insurance companies. Do you foresee any effect on your potential lending pattern as a result of the Canada Pension Plan, which is siphoning off the source of funds available to a number of these, shall we say, conventional mortgage institutions and that they will face year by year a declining volume of money available to them and that the pressure will come on to you, then, to provide the funds for conventional mortgage loans?

Mr. PATON: I do not think I have considered this point, Mr. Lambert. I suppose the answer to that is the ultimate disposal of these Canada Pension Plan funds that are paid to the government.

Mr. LAMBERT: Yes, then they are available for loan to the provincial governments, who are not in the residential financing field.

Mr. PATON: But conversely, if these funds are then passed down to perhaps municipal areas, and replace bank loans to these municipalities, municipal areas, school districts etc., then the funds that would come back into the banks from sources such as these would then be available for other forms of bank lending.

Mr. LAMBERT: I see.

Mr. PATON: Do you have anything to add to that Mr. Coleman?

Mr. COLEMAN: You have the mortgage lenders as well.

The CHAIRMAN: What about if this money is dispersed individually by the municipalities and is deposited in your bank?

Mr. COLEMAN: Then certainly that would be available for lending generally.

Mr. LAMBERT: Well, I think that is the only outstanding question I had insofar as the facilities for mortgage lending are concerned.

The CHAIRMAN: Mr. Cameron.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Paton, I wonder if you have any figures showing the participation of the banks in NHA lending from its initiation? The banks started a new report from 1960 on.

● (5.45 p.m.)

Mr. PATON: I have some figures here on insured residential mortgages of the chartered banks dating back to 1954 as a percentage of our total Canadian dollar loans and as a percentage of our total Canadian dollar deposits. On December 31, 1954, when we initially went into residential mortgages we had outstanding \$74 million, which represented 1.8 per cent of our Canadian loans and .8 per cent of our Canadian deposits. This increased steadily to a peak in 1959 of \$968 million, which represented 15.8 per cent of our Canadian dollar loans and 7.9 per cent of our Canadian dollar deposits. In 1960 there was actually \$971 million, and that represented a declining percentage of 14.9 of our loans and 7.5 of our deposits, and the percentage has steadily decreased. As you are aware, our participation was stopped in 1959-60, when the NHA rate went up over 6 per cent and, according to our legal advice, effectively precluded us from continuing in this area. These totals from principal repayments have gradually decreased, and my figures here for 1965 show outstanding mortgages of \$815 million, which represents 7.2 per cent of our loans and 4.4 per cent of our deposits.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): According to the Bank of Canada reports from August of this year it was down to \$795 million.

Mr. PATON: That is correct. I have just been handed that figure.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Paton, can you tell me when the ceiling is raised, as one gathers it will be, to approximately 7½ per cent, will the banks then be re-entering the NHA lending field to the same capacity they did at the peak in 1960?

Mr. PATON: We will be re-entering it but whether or not to the same capacity, I do not think I am qualified to say. At the present time, assuming that the NHA rate remains as it is at 6¾ per cent, this would still make an attractive investment for the banks in NHA mortgages, particularly when they are conjoined with operating loans to a builder who is a customer of the bank.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): This would not necessarily apply to the individual NHA builder who is building his own home with, perhaps, an individual contractor to build his home for him, rather than a custom builder building a number of houses.

Mr. PATON: It would apply equally.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It would apply equally.

Mr. PATON: The owner of the home might be a valued client of the bank and therefore would arrange his mortgage direct with the bank and have his home built by a builder who builds to order on a custom basis.

The CHAIRMAN: Mr. Cameron, I think there may be something which should be clarified. Am I not correct, Mr. Elderkin, in saying that clause 91 (6) permits the bank to loan money on security of real property at any rate of interest, and that it would not be limited by the maximum rate formula?

Mr. PATON: The NHA has a fixed rate.

Mr. ELDERKIN: The NHA factor would limit the interest rate on those loans.



The CHAIRMAN: Yes, but it is not the Bank Act itself, that is what I am getting at.

Mr. ELDERKIN: No, it is the N.H.A.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then this brings me to my other point. It is this subclause (6) of clause 91 which now disturbs me a little bit, as to whether or not that will not effectively shut out the banks' participation to any great extent in N.H.A. lending where they are confined to the  $6\frac{3}{4}$  per cent.

Mr. PATON: You must remember, Mr. Cameron, an N.H.A. loan is a government guaranteed loan.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes.

Mr. PATON: The security behind that loan is superior to a conventional mortgage which is free of any interest rate.

Mr. LAFLAMME: May I ask a supplementary question?

The CHAIRMAN: If Mr. Cameron will yield.

Mr. LAFLAMME: Is it not possible, then, that the banks go into the conventional mortgage loans so they will not have to lend as much as 90 per cent of the total value of the building?

Mr. PATON: It is possible, Mr. Laflamme, but I think we would be conscious of our responsibility to participate in both types of mortgage lending.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Thank you, that is all.

The CHAIRMAN: The next name on my list is that of Mr. Gilbert, followed by Mr. Clermont and then Mr. Laflamme. It is 6 minutes to 6, so I will give Mr. Gilbert the option of saying whether he wants to begin now or at 9 o'clock.

Mr. LAFLAMME: I have only one question to ask.

Mr. GILBERT: Let Mr. Laflamme go ahead and I will start my questions at 9 o'clock.

The CHAIRMAN: Fine.

Mr. LAFLAMME: I would just like to know, and this is in line with the questions Mr. Cameron asked, on this question of getting any ceiling on loans made on immovable properties, as stated in subclause (6) of clause 91, is this not the main reason why there is a ceiling of 10 per cent on the total liabilities which you can lend, as mentioned in clause 75(4)(a)?

Mr. PATON: The limitation there is confined solely to conventional mortgages, that is, residential mortgages other than N.H.A., and the limitation is probably inserted there to ensure that there is not an excessive diversion of funds into this area, Mr. Laflamme. I think that was your question. What was the purpose of this 10 per cent limitation?

Mr. LAFLAMME: When you answered Mr. Fulton a few minutes ago that the average for 1965 was 4.4 per cent, was it for your bank or all of the banks during 1965?

Mr. PATON: That 4.4 per cent related to the total N.H.A. mortgages outstanding held by all the banks. They had \$815 million of mortgages which represented 4.4 per cent of Canadian deposits.

Mr. LAFLAMME: Is it a fact that subclause (6) of clause 91 allows the banks to go into conventional mortgage loans without any ceiling on interest rates?

Mr. PATON: That is correct. There is no ceiling on these rates. There is a limitation on the total amount which we can lend year by year.

Mr. LAFLAMME: This is the reason why there is a limitation?

The CHAIRMAN: If I may interrupt. I hear some suggestions from some of the specialists who are assisting us here and perhaps we might have this clarified. The limitation on the amount which can be loaned is only with respect to what kind of mortgages?

Mr. PATON: Conventional residential mortgages is the only area of this new type of lending in which there is a quantitative limitation.

Mr. LAFLAMME: This does not bear any interest ceiling?

Mr. PATON: These mortgages do not bear any interest ceiling.

Mr. LAFLAMME: Thank you.

The CHAIRMAN: This meeting is recessed until 9 o'clock this evening.

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*(Recorded by Electronic Apparatus)*

TUESDAY, November 22, 1966.

● (9.06 p.m.)

The CHAIRMAN: I see a quorum, gentlemen. We can now resume our meeting. I believe that we were about to give Mr. Gilbert the floor on the general area of mortgage lending.

Mr. GILBERT: Mr. Chairman, I would like to ask Mr. Paton a question with regard to the mortgage lending field. Some have said that this is a very specialized field, and there are problems regarding valuation, terms of repayment, and titles and so forth. In the past, the majority of conventional lending has been done by the trust companies and the insurance companies, and now you are coming into the field. Just how are you going to handle this complex problem with regard to valuation and long term time repayment, when you operate on a branch system?

Mr. PATON: We all have built up experienced, competent, mortgage departments, Mr. Gilbert, as a result of our entry into the N.H.A. field back in 1954. In fact, I would probably be right in saying that each of these departments is champing at the bit ready to get back into the business again, because, as you know, we have been relatively static over the last number of years. However, we have very competent people throughout the various bank divisions, and our branch managers have also been exposed to this type of lending in the past. We have definite instructions on file, and it will not take us very long to get back into that situation of competence again as soon as the freedom is available to us.

Mr. GILBERT: In the N.H.A. field you did not need a valuation department; are you planning on setting up a valuation department now?

Mr. PATON: Yes, but it is not right to say we did not need an evaluation department, because while these mortgages had C.M.H.C. approval; nevertheless the banks were not willing to accept mortgages purely on the basis that they had this approval. We still had our independent appraisals and independent checks made to ensure that they were suitable mortgages for our investment portfolio.

Mr. GILBERT: How would you handle a mortgage, say, in a small town, such as Mr. Fulton referred to today. He is hoping that there will be a spread-out of these mortgage moneys? Just how would you handle a mortgage in a small town? The branch manager would approve the mortgage. Would you have the property evaluated, and how would you handle the accounting aspect?

Mr. PATON: The accounting aspect would be no problem. The evaluation might require some expertise from our divisional office in the relative province; for example in Alberta, the expertise for this area would probably be confined to our divisional head office, either in Calgary or Edmonton. These people would be accessible to any branch manager in the area. I think it is reasonable to say that in any town one can get an evaluation satisfactory for our needs.

Mr. GILBERT: Are the banks accounting records, with regard to N.H.A. mortgages, centralized with the head office, or are they spread out to the different branches?

Mr. PATON: Unfortunately, my expert on mortgages is not with me tonight, and it is not a question I am really competent to answer. Each branch, I know, handles the repayments of the mortgages they have in their books. Today's banks accounting may be somewhat different, but in general I think it could be said that these are centralized either at the divisional level or possibly at head office. But the actual mortgages, and the collection of the mortgages, that is the monthly repayments, are handled by the branches themselves, if for no other reason than that it gives them contact with the mortgagor, and it means an account for that particular branch.

Mr. GILBERT: I would like to direct your attention to clause 75(3), and, Mr. Chairman, I would like to have the help of Mr. Elderkin on this. As I understood his interpretation of clause 75(3) this clause would not prohibit or restrict a bank from taking a second mortgage. I am just wondering if the Canadian Bankers Association contemplate going into the second mortgage business.

Mr. ELDERKIN: I might say, Mr. Gilbert, they can only take a second mortgage within the limit of the 75 per cent evaluation.

Mr. GILBERT: Yes, You are right. In other words, suppose there is a mortgage on the premises for, say, \$5,000, and the lending value amounts to \$10,000, would the bank be prepared to take a second mortgage in the amount of \$5,000?

Mr. PATON: I think it would be entirely possible that they might. It would be subject to the particular requirements on the application, as to what the funds were going to be used for; whether the borrower had the capacity to handle both the first and second mortgage payments. It would not be beyond the realms of possibility that the banks would do so. I do not think it is a form of lending that we are anticipating in any great degree, but certainly the right is there and it will undoubtedly be utilized on certain occasions.



Mr. GILBERT: Probably one of the difficulties that the average home owner is going to find is that he has an N.H.A. mortgage at  $6\frac{3}{4}$  per cent; he may have a second mortgage at say, 10 or 12 per cent, and he may want to consolidate the two mortgages. He has a high first mortgage with N.H.A. at  $6\frac{3}{4}$  per cent, and he has a second mortgage at 10 or 12 per cent. Now the ideal situation would be that the bank would be permitted to re-finance under the N.H.A. to consolidate the two mortgages at  $6\frac{3}{4}$  per cent, once that first mortgage comes down to an amount to absorb the second mortgage. However, the ordinary person cannot do it; in fact, the National Housing Act does not permit it. So, you are going to find yourself in a position where there are two mortgages on the premises, and with your conventional loans at 8 or  $8\frac{1}{4}$  per cent the N.H.A. owner is going to find himself losing the low interest rate of  $6\frac{3}{4}$  per cent to absorb the second mortgage at 10 or 12 per cent. What are your comments on that?

Mr. PATON: Your hypothesis is that there is an existing N.H.A. mortgage for \$5,000, that he wishes an additional mortgage for another \$5,000, and that the loan value of the house would permit this total lending of \$10,000.

Mr. GILBERT: Well, that is one example, yes.

Mr. PATON: It would, of course, be supposed that with that \$5,000 new money he is getting he is going to—

Mr. GILBERT: He is going to discharge an existing second mortgage at 10 or 12 per cent.

Mr. PATON: Oh, he already has his first and second on it; the total indebtedness on this property is \$10,000.

Mr. GILBERT: That is right.

Mr. PATON: Five thousand dollars of which he is borrowing at 12 per cent, and \$5,000 at the current rate, and he comes to a bank to suggest that he would like to combine these two mortgages into a first mortgage?

Mr. GILBERT: That is right.

The CHAIRMAN: Just to clarify, are you suggesting that this new first mortgage cannot be under the National Housing Act?

Mr. GILBERT: Mr. Chairman, the existing first mortgage is under the N.H.A. at  $6\frac{3}{4}$  per cent; and the second mortgage rate prevails at either 10 or 12 per cent. The owner wants to consolidate the mortgages; he is then faced with the problem of being forced to obtain a conventional loan at 8 per cent or  $8\frac{1}{4}$  per cent, and lose his low interest rate under the N.H.A. at  $6\frac{3}{4}$  per cent.

The CHAIRMAN: I think you have a very good point. I just wanted to mention that it would appear from the amendments to the National Housing Act that were just passed, that if the person had just bought the home—

Mr. GILBERT: No; that amendment restricts itself to the purchase of an improvement in an occupation.

The CHAIRMAN: Yes, well that is what I am talking about.

Mr. GILBERT: I am not talking about this; I am talking about a person who buys a house and five years later that N.H.A. mortgage has come down to a

position where it is possible to absorb the second mortgage into a first mortgage. He is now going to be placed in the position of losing his low interest rate on the N.H.A. in order to consolidate his mortgages.

Mr. PATON: In other words, he cannot get an N.H.A. mortgage for the full amount under the present regulations of the N.H.A., on the example that you are citing; his only alternative would be to get a conventional mortgage for the \$10,000, which would necessitate him, presumably, paying the going rate of 8 percent or  $8\frac{1}{4}$  per cent.

One cannot make a blanket statement, when asked for comments on that, Mr. Gilbert. Each individual case would have to depend on the circumstances surrounding it. For example, if this individual's financial affairs had developed in the five or six years that he has been paying on his N.H.A. mortgage to a stage which would adequately warrant him repaying a mortgage of \$10,000 on a first mortgage basis; it is conceivable that a bank would take a conventional mortgage, as they cannot take an N.H.A. But I see no alternative to the borrower, other than to pay the going rate for conventional mortgages on this basis.

Mr. GILBERT: What I am saying to you is that Mr. Elderkin said that you can involve yourself in second mortgages, and the simple solution to a problem like that would be to permit the owner to leave the existing first mortgage at  $6\frac{3}{4}$  per cent, and obtain a second mortgage from you at, say, 8 per cent; thereby avoiding the 10 or 12 per cent. Because if a conventional mortgage goes on, all you are doing is that you are having the owner move up from the  $6\frac{3}{4}$  per cent to 8 or  $8\frac{1}{4}$  per cent, and then he is coming down from the 10 per cent or 12 per cent to  $8\frac{1}{4}$  per cent; so he is not gaining too much in the circumstances.

Mr. FULTON: Would it not be purely a business deal from his point of view? If he can consolidate his two loans at an average interest slightly lower than the sum of the two he is paying, would it not be to his advantage, if he can get the banks to agree?

Mr. GILBERT: Mr. Fulton, that depends on the ratio of the first and second mortgage.

Mr. FULTON: Yes. It would be a business deal though, which is to his advantage.

Mr. CAQUETTE: Well, on the one hand, he is losing, and on the other hand, he is gaining.

Mr. GILBERT: All I am saying to you, Mr. Paton, is that the preferable treatment to a home owner would be to permit him to leave the existing first mortgage on, and re-finance the second mortgage with you.

Mr. PATON: But, Mr. Gilbert, if the going rate for first mortgages at the time this request is made, is 8 per cent, then automatically second mortgages would attract a higher rate than 8 per cent, not necessarily 12 per cent, but a higher rate than 8 per cent. And if the bank is not the holder of the original N.H.A. mortgages there would be no incentive to the bank to lend on a second mortgage security at 8 per cent to this individual when there are others applying for first mortgages who are equally entitled to them, and the bank could take first mortgage security at the same prescribed rate for the purpose. In other words, as Mr. Fulton said, it would be strictly a business transaction between the borrower and the bank.

The CHAIRMAN: Do you have any further questions?

Mr. GILBERT: I think that is all, Mr. Chairman, thank you.

The CHAIRMAN: Well, Mr. Lind, I think is the only other person who has signified that he wishes to speak.

Mr. LIND: I would like to draw your attention, Mr. Paton, to the condition that existed in the 1954 to 1959 era throughout some of the rural areas. Although the banks were in the loaning field, the favorite answer of some of the local managers was, "well, I do not have the staff to handle N.H.A. accounting". When we went after them to get the staff, they said it would cost them more to pay an extra man to do the accounting than it was worth. Now, is this same condition going to exist again if you go into the N.H.A. field?

Mr. PATON: I would not like to accept your statement that this was common, Mr. Lind. I would suggest that if this particular situation did occur, or had occurred, it would have been a very good thing to advise the bank concerned—the head office of the bank—that this was the type of reply you had received. Managers, being human, have different receptive attitudes towards new ideas or new lending. In any type of specialized lending, the first loan you put in your books takes longer to record than the normal type do; but as you gain experience there is no problem to handling the accounting. This particular reaction, that you referred to, I hope would be the exception and not the rule.

Mr. LIND: Well, you should know from your experience whether there were many N.H.A. loans issued in rural areas.

Mr. PATON: I have no figures; but I know, for my own bank and I am sure I speak for the others, that in relation to the applications from these areas, the percentage of acceptances would not be very far removed from any other area, even the major areas. The volume would not be there, because the volume of requests would not be there.

Mr. LIND: No, but you are sure that some have been processed in rural areas, are you? I am concerned with the small villages and towns away from the built up centres, where it was rather hard to get N.H.A. loans through the banks, although they had branches there from 1954 to 1959. On consultation with many of the building supply dealers throughout the province of Ontario, I find they found the same conditions.

Mr. PATON: In our brief, Mr. Lind, you will notice that we say "however, participation by the banks would lead ultimately to a more competitive rate structure for mortgage loans, especially in areas of the country already served by banks, but where institutional mortgage lenders are not represented". We did not put that down lightly, and I think the banks would be prepared to stand behind that comment.

The CHAIRMAN: Mr. Lambert has a supplementary question.

Mr. LAMBERT: Just on that point, it seems to me that some time in the past I ran across some information to the effect that when the banks were at their peak lending, under the N.H.A. almost 50 per cent of the loans they were making were in communities of 50,000 or less. Am I correct in that information?

Mr. PATON: I am not sure; I could not confirm it. I have not heard that percentage, and I do not know whether any of the others have.



Mr. COLEMAN: I cannot add anything to it.

Mr. PATON: It would not surprise me, Mr. Lambert, if that were true; areas with a population of 50,000 and less.

Mr. LAMBERT: Yes, then this would be germane to what Mr. Lind said, except that it presents a different picture; he may have run into one spotty area.

Mr. PATON: The Central Mortgage and Housing Corporation people could answer that question.

Mr. FULTON: They would not be coming here, Mr. Paton, to discuss this act.

The CHAIRMAN: Perhaps Mr. Lind might consult with one of our research officers to see if the Central Mortgage and Housing Corporation can provide some type of information.

Mr. LIND: I would like to go on, if I may, with another example from the area. Suppose the conditions are ideal and the banks have plenty of deposits, and they are looking around for mortgages. A home that was built, say, 13 years ago is resold, which is not uncommon and if it had cost \$10,000 to build originally, it is sold now for \$16,000 or \$17,000. Let us say, there is a mortgage on it by one of your competitors, or the near banks. Would it be the policy of the bank to help this fellow out if he wanted to re-finance, maybe on a resale, and go in and probably loan \$10,000 on a first mortgage?

Mr. PATON: The banks would appraise this property at its current valuation, not at the purchase price. Therefore, a loan of \$10,000 on the instance you cited would be a reasonable loan, and would qualify—

Mr. LIND: Well, that would still be well under 75 per cent.

Mr. PATON: That is correct.

Mr. LIND: The selling price is usually within a reasonable striking distance of the current value price, is it not?

Mr. PATON: Yes, and the banks appraise their lending ability on the current value, rather than on the original purchase price.

Mr. LIND: You would assume then that the banks would go in and help the person out, provided he is only pledging 20 per cent of his monthly earnings towards the payments, including interest, principal and taxes.

Mr. PATON: That is a very low percentage, according to my recollection of N.H.A.

Mr. LIND: Now suppose, there is an open-end mortgage in there for \$5,000, what would be your policy?

Mr. PATON: One mortgage?

Mr. LIND: And your bank held the open-end mortgage, would you increase it to \$10,000?

Mr. FULTON: How would you get it in the first place "already"?

Mr. LIND: If he had it already.

Mr. FULTON: How would he get it?

Mr. LIND: Well, they may have an old NHA mortgage.

Mr. FULTON: That is not an open-end mortgage.

Mr. PATON: I am not sure what you mean exactly by an open-end mortgage?

Mr. LAFLAMME: I doubt whether there is any open-end mortgage in Canada.

Mr. FULTON: Not under NHA, and that is the only kind you would have up to now, is it not?

Mr. PATON: Up to now, yes.

Mr. GILBERT: Mr. Chairman, what does he mean by an open-end mortgage?

The CHAIRMAN: I was going to suggest to Mr. Lind that he define what he has in mind so we can be sure we are all thinking of the same thing.

Mr. LIND: An open-end mortgage, in my estimation, and they do exist as private mortgages, is one that can be enlarged, or added on to the end if there are additional repairs or improvements put on the building; say they put \$10,000 into improvements, then they could put a \$3,000 or \$4,000 addition on the end of the mortgage.

The CHAIRMAN: Do you mean at the instance of the borrower?

Mr. LIND: No, they do not have to re-issue a new mortgage in my understanding.

An hon. MEMBER: I have never heard of that.

Mr. PATON: I cannot visualize us getting into that type of mortgage, Mr. Lind. I presume that a mortgage would not have a fixed monthly repayment basis, of this nature, or conceivably it could have. I do not think the instances of such mortgages would be material.

Mr. LIND: They are not too common at the present time.

Mr. PATON: Would it not be the result of negotiation between a private lender and a private borrower?

Mr. LIND: Not necessarily, there are institutional mortgages that are open-end mortgages.

Mr. FULTON: Kindly give me the name of the lender, will you?

Mr. LIND: Yes, I will give it to you. Now, there is one other question I would like answered. This afternoon you made a statement about how you could help out the construction business, where you were probably giving a construction man some accommodations through a current account. If you were giving him a loan for home construction, you could probably give him better accommodation through his current account. Now, what if this man gets into trouble, and you have asked for the assignment of the mortgage as a guarantee to your current account, and some of the suppliers who may be had to lien in order to protect their interests—possession of the money sometimes means about nine-tenths of the law—what would happen in a case like that?

Mr. PATON: There is a trust clause in the mechanic's lien act, and I think perhaps this is one of the subjects Mr. Lambert alluded to it when the Inspector General or the Governor was on the stand. But the normal procedure in lending

to a contractor of that nature is to take an assignment of the mortgage commitment, assuming that the mortgagee is somebody other than the bank. You take as assignment of the mortgage draws. These mortgage commitments sometimes are single pay-outs which are made when the property is completed. Other mortgage commitments are on a progress draw basis. As the work progresses to a certain stage a percentage of the total mortgage is remitted.

It is the bank's responsibility, if they are lending money to this individual, to see, in their own interest, that his payments to his supplies are kept up to date. If the contractor gets into trouble, and the bank has not been able to perhaps prevent him from doing so, through lack of supervision, or some other reason, then there is a possibility of problems, there is no question about that.

Mr. LIND: Have you sufficient personnel to do the four inspections on these in all these rural areas at the present time, if you go into this loaning field?

Mr. PATON: We would not presume to make inspections; now, mind you, if it were under NHA, the payments are not forthcoming unless the CMHC inspector approves the draw. In financing a contractor, we would not inspect as a regular procedure every residence he is constructing.

The CHAIRMAN: Do you have any further questions, Mr. Lind? If not, I will recognize Mr. Fulton.

Mr. FULTON: Mr. Chairman, there are just two matters I would like to mention. First, there is a correction for which I apologize to the Committee for having to make. At the afternoon session, when I was asking Mr. Paton about the extent to which the bank felt they might get into this mortgage lending field, I said I had been provided with figures which indicated that the institutional lenders had withdrawn in 1966, as compared with 1965, to the extent of \$850 odd million. I had misread my figures. I think I was speaking of the total mortgage lending business; whereas I implied that I was speaking of residential mortgages. I think if I correct my figures that it would be more like \$300 million, as between 1965 and 1966, on the residential business. Therefore, having given you a figure of \$850 million—and I recall that I asked you to what extent you thought the banks might make up the deficiency under the new proposal—I have given you a totally wrong impression. I make my correction with apologies, and I wonder if you would like to make a correction to your answer.

Mr. PATON: I think I hesitated about putting a figure, Mr. Fulton, taking your \$800 million as factual, and during the recess it was pointed out to me that your figure was not correct; this area of \$300,000 is more accurate.

Mr. FULTON: It is million.

Mr. PATON: Pardon me, I guess it is getting a little late; \$300 million—

Mr. FULTON: We can both be wrong about that.

Mr. PATON: Yes, we certainly can. I would still say that we could make a considerable indentation in that \$300 million figure. I would hesitate to say that we would completely replace the full amount, but I think we could make a fair impression on that deficit.

Mr. FULTON: I take it, Mr. Paton, that you do not care to give a percentage I have pursued this with you before. With respect to policy, I spoke about the



smaller communities and so on. Subject to the correction of percentages, and so on, the policy position remains as you described it to me before?

Mr. PATON: I would say that subject to the bill, the figure of \$300 million, would not scare us at all in thinking that we could replace this deficit in the amount of lending. Witness the extent that we went into NHA, when we were able to do so.

Mr. FULTON: Yes. Thank you. The other point I have to ask you, and I am afraid it is a technical one, has to do with clause 75(3). I raised this matter, I think, when Mr. Elderkin was giving evidence here, particularly with respect to British Columbia. As I understand it, it seems to be assumed that under clause 75(3) the banks may make advances upon second mortgages. My question to Mr. Elderkin was whether this was applicable to British Columbia, because of the wording of the subclause. As I appreciate the law in British Columbia, a second mortgage is not taken upon the security of real or immovable property, but rather upon the equity of redemption. Mr. Elderkin said that they would have a look at that, and I am wondering if you, or your solicitors, have had a look at this so far as British Columbia is concerned.

Mr. PATON: I think that question has been looked at since you raised it originally, Mr. Fulton. Mr. Cate is with us. Did he have an opportunity to discuss this with you, Mr. Elderkin?

Mr. ELDERKIN: I discussed this with justice Mr. Chairman, and there are at least two provinces in which there are no second mortgages on real or immovable property; one is British Columbia, and Ontario, I think, has a similar law. What you get in place of that is a mortgage on the right of redemption, and the result is exactly the same; but it is on a different type of security.

Mr. FULTON: Yes. Therefore, my question is simply, if the banks are to be allowed, that is, if the intent is the banks may advance money on a second mortgage, do you think we require rewording of this section in order that you may do it in British Columbia, which we would like you to do.

Mr. ELDERKIN: Again, if I may interject, I asked the same question of the draftsman of the Department of Justice, or rather the legislation section of justice, and they felt it was not necessary to amend here.

Mr. FULTON: I have the greatest respect for your opinion, and for the opinion of the Justice Department, but I am wondering if the banks who are going to have to make the advances have consulted with this legal counsel.

Mr. ELDERKIN: But in any case, may I add, that the banks can, under the other provisions, take security on personal property. This is, I believe, if I understand it correctly, Mr. Fulton, where the redemption is personal property, and not real or immovable property. So, they could lend on personal property without limitation.

Mr. PATON: We have not obtained a firm opinion from our association's solicitor but we have discussed it with him and I would undertake to have an opinion from him prior to the ending of these hearings; or our appearance here. If the ending of our appearance occurs before the hearings are over.

Mr. FULTON: Thank you.

Mr. LAMBERT: Mr. Paton, you have served out in Alberta and I am sure you are aware of the provisions of section 34 of the Judicature Act in that province, which, in effect, limits the right of recovery to the value of the security. In other words, the personal covenant is being eliminated in all types of mortgages by NHA mortgages. As a matter of fact, when the NHA legislation first came in just after the war, they passed a special provincial act to create the exemption for that. Now that the banks are going to be allowed to go into the conventional mortgage lending field, I would think that you will have your people look very hard at this situation and that the Alberta government will have to look very hard at this situation in order to place the business in that province on an equal footing with the rest of the country. I know that as a result of a certain action involving one of the conventional mortgage companies, recent legislation was passed to outlaw any specific waiving of this protection against personal covenant, but I see that we are heading for trouble. You might have your solicitors look at that to confirm my view that the banks will be seriously circumscribed in the province of Alberta with regard to lending on conventional loans either for residential or commercial purposes.

Mr. PATON: We will take note of that, Mr. Lambert.

*(Translation)*

Mr. LATULIPPE: Could you give us the three main reasons which have caused the Government to forbid the banks to enter the mortgage field for a number of years?

*(English)*

The CHAIRMAN: Mr. Paton, can you deal with that or would you like me to ask Mr. Elderkin to provide some of the background?

The question, as I understood it, was what seemed to be the thinking which led to the law originally in not permitting banks to lend money on mortgage security.

Mr. ELDERKIN: I think it came actually at the time of confederation from the practice in the Scottish banks as much as anything else, who—

The CHAIRMAN: You mean you did not want to answer that?

Mr. PATON: I did not want it to appear that I would be boasting, therefore I referred it to Mr. Elderkin.

Mr. ELDERKIN: And it was felt, at that time and for a great many years afterwards, that banks should not be in long term assets which were not readily negotiable. The mortgage business today is an entirely different one from what it was a few years ago. I would think that if we went back to the thirties you would find that most of the mortgages were written with no interim payments during their period but almost entirely payment in full at maturity. Now practically every mortgage is written with periodic payments to maturity. If you start off with a 75 per cent valuation and you have periodic payments of monthly or quarterly or even annually, it is probable that before any serious difficulty can arise in that particular loan that the loan has been paid down to a point where it is not difficult to recover the value of the security.

(Translation)

Mr. LATULIPPE: We should point out, Mr. Chairman, that it is not the financial system which fails in Canada, I think this is the most prosperous of all systems, I do not think we should let things stand as they are, we should correct what is going wrong. Could you tell us, then, why up to now, the Government has imposed special legislation in respect to banks only, why were you prohibited by Government action to lend at more than 6 or 7 per cent, or make mortgage loans? Why did the Government prevent you from accumulating capital through debentures? Why did he prohibit you from having various types of shares, as all other companies have? "A" class shares, "B" class shares, "C" class shares, common shares, and so on and so forth, and not only even without par value, could you answer that question?

The CHAIRMAN: I think you have a series of rather knotty questions, these are obviously very important matters, but I believe that except for that question which referred to mortgage loans, this matter does not come under the topic we are discussing at the present time, I believe indeed that Mr. Elderkin has just answered your questions in respect of mortgages and I suggest that such other questions should be withdrawn under some other and further period, because they do not come under the topic we are discussing at the present time, which is mortgage loans.

Mr. LATULIPPE: But I would like to know why all these prohibitions have been put in your way? Why were such prohibitions imposed on banks by the Government? Why have banks remained silent up to now?

The CHAIRMAN: Your question is a good one perhaps, but here again I must indicate that it would be far better to put these questions to the minister, when he will be here, because his responsibilities bear very close to relationship to general policy matters. As far as prohibitions imposed on mortgage lending, I believe that we can say that Mr. Elderkin has answered this satisfactorily, he has explained why it was not allowed up to now for banks to make mortgage loans. However, the other questions important as they are admittedly, though I might be wrong, do not come under this general topic of mortgage loans. Perhaps you could keep these interesting questions for a later date.

Mr. LATULIPPE: Mr. Chairman, if such prohibitions have been imposed by Government action on banks, this appears to be rather peculiar, there must be serious reasons for this, I would like to know what these reasons are.

The CHAIRMAN: Of course, you have every right to ask for reasons, but I think this is a matter of policy which comes under the Minister, or some elected representative of the people authorized to make such policy alterations. I do not think it is quite fair to question Mr. Elderkin, who is an official of the Government, on policy matters and I do not think that you should put those questions to our banking friends either. I do not believe you could ask for comments or ideas on policy matters which deal with matters previous to the presentation of this bill.

Mr. CAQUETTE: Could I put a supplementary question? Yet, you have just said, was it not a cardinal principle of banking policy not to go in mortgage loans until now? This was not so much a matter of government policy, but ten, fifteen,



twenty years ago banks were not interested in going into the mortgage loan field, is this true, Mr. Paton?

The CHAIRMAN: I wonder if it is proper to make comments on banking policy. Perhaps you can comment on the attitude of the industry until now or before now?

*(English)*

Mr. PATON: I would agree, Mr. Chairman. I think this is hardly a question on which I should comment, but I would say that I feel that Mr. Elderkin's reply to Mr. Latulippe covered the difference between mortgage lending in the past and mortgage lending today. This is an evolving economy we are in and we operate under an entirely different approach to the suitability of bank investments, under present day operations.

Mr. CAOUPETTE: It is not merely the government's policy, it is, at the same time, the banking system's policy.

Mr. PATON: There is very little difference between the two.

Mr. CAOUPETTE: Yes, I know what you mean.

The CHAIRMAN: I presume you mean that the banks are following the policy laid down by the government?

Mr. PATON: I did not think I was required to elucidate.

*(Translation)*

The CHAIRMAN: Mr. Latulippe, would you have any questions to put?

Mr. LATULIPPE: Yes, could you tell me if banks issue financial credit based on the value of real credit of the borrowers, or if this is based on the value of the goods they possess?

The CHAIRMAN: You mean we are dealing with mortgage loans here?

Mr. LATULIPPE: Yes.

Mr. LAVOIE: You are speaking of mortgage loans or commercial loans at this point?

Mr. LATULIPPE: Mortgage loans?

Mr. LAVOIE: Well, as we stated a while ago, banks have not been in this field, except a few years ago. A few years ago, we did make mortgage loans under the N.H. Act. However if we do enjoy this right, henceforth it will be based on the actual value of the property. We will not be allowed to lend at more than 75 per cent of the value of the property.

Mr. LATULIPPE: What about commercial loans?

Mr. LAVOIE: But up till now we did not have authority to make mortgage loans except in very peculiar cases—that is to obtain further security for a loan which has already been made, that was allowed. In future, I believe that if the authority is given to us, it will be possible for us to make loans, even commercial loans. In a small community, I understand that a merchant or an industrialist does not perhaps have other sources of financing. If then, he can obtain money from a bank, partly through a mortgage loan, partly through a commercial loan to improve his operating fund, and the other part to transact business, this will be of considerable assistance to this small industrialist or this small tradesman,

who lives in a small community where mortgage loans or commercial loans are on occasion rather difficult to obtain without security.

Mr. LATULIPPE: Could you tell me if in practice, these advances will be made in a proportion of eight against one, that is for each dollar of reserve you have in your account, the bank will be able to lend eight dollars, is this policy going to continue?

Mr. LAVOIE: I believe, Mr. Latulippe, the banks will continue to make commercial loans under the same conditions as has been done up till now, based on the credit rating of the customer and on such repayment conditions as could be required.

Mr. LATULIPPE: One eighth of the money thus advanced is provided by the shareholders, the seven other eighths consisting in bookkeeping entries, is that what you call Canadian money?

The CHAIRMAN: Mr. Latulippe, here again you are dealing with a matter of general economic policy. This is no doubt a very interesting matter, but may I suggest once again that we have perhaps wandered a little too far away from this matter of mortgage loans.

Mr. LATULIPPE: In this case, could you tell us what is the real security of that money?

The CHAIRMAN: What money?

Mr. LATULIPPE: This money you lend out in mortgage loans or commercial loans. What is the real security for this money?

The CHAIRMAN: You are speaking of mortgage loans here, are you not? Well, the banks might answer, but the question is obvious, is it true?

Mr. LATULIPPE: Who provides the security, the borrower or the bank?

Mr. LAVOIE: Well, the borrower, of course.

Mr. LATULIPPE: But the bank puts only its 8 per cent, the rest comes from the borrowers, so frankly the bank does not provide too much.

The CHAIRMAN: I think that we could reflect on that a little bit.

*(English)*

I am going to ask the Committee to consider a point of procedure.

Does the Committee wish to sit beyond 10 o'clock? Perhaps we could finish the topic of mortgage lending. It is 10 o'clock now, the usual adjournment hour.

Mr. FULTON: I missed your question; I am sorry.

The CHAIRMAN: I was going to ask if the Committee wishes to sit beyond 10 o'clock?

Mr. FULTON: Can we do it in 15 minutes?

The CHAIRMAN: Let us say we will sit for 15 minutes. I think you have a very good suggestion. We will sit for 15 minutes and see if we can finish.

*(Translation)*

Mr. GRÉGOIRE: Mr. Chairman, do you mean to say that in fifteen minutes, we will have to leave this topic of mortgage loans whether we are through or not or

does it mean that whether we are through or not we will adjourn? I have not said a word about mortgage loans, do you really mean to say you can finish in fifteen minutes?

The CHAIRMAN: Mr. Grégoire, as we say in English.

*(English)*

Levity is the soul of wit. You might be able to test that ancient saying for us.

I want to point out that the question of mortgage lending came up during our initial general round of questioning and I gather it is the intention of the Committee, once we have a period of specific questioning on the issues, that we have, if necessary, some further general questioning at some appropriate period if that is the wish of the Committee before we complete our study of the bills.

*(Translation)*

Mr. GRÉGOIRE: I have only one question to put on that.

The CHAIRMAN: Has Mr. Latulippe finished?

Mr. LATULIPPE: Well, I could let other people put questions, I might return to this matter to-morrow.

The CHAIRMAN: To-morrow?

Mr. LATULIPPE: Or later.

The CHAIRMAN: On mortgage loans or general matters?

Mr. LATULIPPE: On mortgage loans and on general matters. However for the moment, I will pass.

The CHAIRMAN: Mr. Grégoire.

Mr. GRÉGOIRE: Are we starting on the second round, now?

The CHAIRMAN: It is one of the rounds.

Mr. GRÉGOIRE: I was waiting for the first round to come around to me.

The CHAIRMAN: Your turn will come, we must wait for all good things in life.

Mr. GRÉGOIRE: Well, we are starting on the second round, are we not?

*(English)*

The CHAIRMAN: Well, any way, Mr. Lambert.

Mr. LAMBERT: My question has reference to clause 75 (6). It has to do with the relationship with insurance companies or restriction. Do the banks have any limitation upon the types of insurance companies they will consider as insurers with regard to any mortgages that they may enter into? I know that some conventional lending companies, for instance, would have nothing to do with mutuals; they want board companies. Is there any restriction at all among the banks as to what insurance companies they will take policies with with regard to their mortgages.



The CHAIRMAN: Are you in a position to deal with this question?

Mr. PATON: I do not think Mr. Lambert, that I am, factually. It has really been a long time since I have taken a look at that. I know in my practical banking experience when I was in a branch that I was very conscious of the company with which the insurance was placed on any security I had. I would think that there is some basis of acceptance but frankly I would like to take that question under advisement and find out.

Mr. LAMBERT: You might want to take that as notice.

Mr. PATON: I would like to very much because it is a very good question.

Mr. LAMBERT: Thank you, that is fine.

(Translation)

Mr. GRÉGOIRE: Mr. Chairman, in that part of your brief where you deal with mortgage loans, page 6, you say that "since 1954 chartered banks have been allowed—" What then has prevented the banks from making mortgage loans under the National Housing Act? Was there an Order-in-Council which set the minimum interest at a higher rate than 6 percent?

Mr. LAVOIE: That is true, Mr. Grégoire.

Mr. GRÉGOIRE: Well, therefore, would it have been possible for the banks to make mortgage loans under the N.H.A. simply by repealing that Order-in-Council instead of raising the ceiling on the interest rate? Would it have been possible for the government to do that?

Mr. LAVOIE: The Bank Act sets the maximum rate at 6 percent. It is therefore impossible for us to make mortgage loans.

Mr. GRÉGOIRE: But because of the Order-in-Council you have mentioned. But had this Order-in-Council been amended so that the minimum rate of interest would not have been set for chartered banks, and if the chartered banks alone were provided for under this Order-in-Council, had it been repealed, would it have been possible for you to make any loans at 6 percent?

Mr. LAVOIE: We have obtained an opinion from our counsel. We were told that the Bank Act had priority here.

Mr. GRÉGOIRE: Is there an Order-in-Council fixing interest rates at  $6\frac{3}{4}$  percent but affecting only chartered banks or savings banks? Trust companies were not affected because there is no ceiling as far as their interest rate is concerned. But chartered banks were. Now, let us assume that this Order-in-Council would have been amended or would be amended in such a way that chartered banks would not be obliged to keep under this minimum rate of  $6\frac{3}{4}$  percent.

The CHAIRMAN: But this is not the minimum rate. This is the maximum rate.

Mr. GRÉGOIRE: This is the minimum too, because if it were the maximum rate—

Mr. LAVOIE: The maximum is  $6\frac{3}{4}$  percent.

The CHAIRMAN: It is.

Mr. GRÉGOIRE: But what Act prevented you from lending on mortgages at 6 per cent?

(English)

Mr. PATON: At 6 per cent or over 6 per cent?

Mr. GRÉGOIRE: At 6 per cent.

Mr. PATON: You are suggesting that when the current rate was  $6\frac{3}{4}$  or in excess of 6 per cent that the banks still could have loaned at 6 per cent? That is correct. The banks could have loaned at 6 per cent but automatically had they, getting back to Mr. MacIntosh's statement this afternoon, the exercise would have resulted in every new N.H.A. mortgage falling into the bank's portfolio. If we had indicated our willingness to continue lending on N.H.A. mortgages at 6 per cent which we could have done, and the other lenders were lending at  $6\frac{3}{4}$  per cent, obviously the banks would have been flooded with applications to lend at 6 per cent which would be quite uneconomical.

(Translation)

Mr. GRÉGOIRE: But then you would have attracted customers, would you not?

(English)

Mr. PATON: We would not have stayed in business long enough to keep them.

(Translation)

Mr. GRÉGOIRE: What about the other assets you have? What about your other deposit liabilities? Were you not lending these out at 6 per cent, at the same rate? What is the difference between lending at 6 per cent on a non-mortgage loan and at 6 per cent on a mortgage loan, from the point of view of income?

(English)

Mr. PATON: There is no difference from the point of view of income, Mr. Grégoire, but there is a vast problem with respect to our available resources.

(Translation)

Mr. GRÉGOIRE: Does this mean that you did not want to make long-term commitments? Is that what prevented you from lending out?

(English)

Mr. PATON: No, sir. I think our performance in the N.H.A. mortgage field where we acquired the figures I quoted to you this afternoon would indicate that we were more than willing to participate in this type of lending when we had the opportunity to do so.

(Translation)

Mr. GRÉGOIRE: Now, Mr. Chairman, in Section 91, sub-Section 6, we told that: "the maximum rate of interest or rate of discount prescribed by this section does not apply where the bank a) lends money or makes an advance on the security of real or immovable property in Canada, including an assignment of or mortgage on the interest of a lessee of real or immovable property." This means that there will be no ceiling on the interest rate when will have a mortgage loan.

Mr. LAVOIE: Yes.

Mr. GRÉGOIRE: In other words, if the Act were voted to-night as the average yield on bonds is at present  $6\frac{3}{4}$  percent, in respect of an ordinary loan, you would lend out at 7 percent but on mortgage loans you may lend out at (8 percent). You could do that to-morrow if the Act were passed to-night? It is obvious, then, that it means 1 percent interest more if it is in the form of a mortgage loan.

Mr. LAVOIE: Yes.

Mr. GRÉGOIRE: Does that mean that if the Act were adopted tonight since the yield on short term bonds is now  $5\frac{1}{4}$  percent, you will make an ordinary loan at 7 percent and the mortgage loan at 8 percent? That means that the banks get 1 percent interest more when the loan is a mortgage loan. On \$18 or \$19 billions—

Mr. LAFLAMME: But there is a maximum of 10 percent.

Mr. GRÉGOIRE: If these are on N.H.A. mortgages.

Mr. LAFLAMME: But under the Act, there is a 10 percent limit under sub-section (a) of Section 75.

Mr. GRÉGOIRE: But does this involve conventional mortgages also?

Mr. LAFLAMME: Yes.

Mr. GRÉGOIRE: But as far as that 10 percent is concerned, does it mean that chartered banks will feel more like lending out in mortgage loans at this unlimited rate than at the other rate provided under the Act?

Mr. LAVOIE: I do not believe that the banks would like to lend out more under mortgages as long as they want to remain in their original area, that is, commercial loans. They will, however, add mortgage loans to that. It will depend on their resources.

Mr. GRÉGOIRE: But the fact that you will be limited to 7 percent in respect of commercial loans because of this transition period, and because of the fact, too, that there is no limit as far as mortgage loans are concerned, you may go up to 9 percent. Will this 1 or 2 percent constitute an adequate interest for the bank? Is that not an inducement for you to make mortgage loans?

Mr. LAVOIE: If you refer to 75.4, you will see that chartered banks are limited under the Act. For the first year, it is 2 percent. Then we have 1 percent yearly up to 10 percent.

Mr. GRÉGOIRE: And as far as this 10 percent is concerned, will it be to the advantage of banks to reach this 10 percent maximum since this will bring in a greater interest rate?



Mr. LAVOIE: It will depend on our resources. It would take ten years for the chartered banks to reach the maximum of 10 percent they are authorized to lend under this mortgage provision in the Act.

Mr. GRÉGOIRE: But whatever the number of years, inevitably since the ceiling would have been removed, this will be an inducement for the banks to make mortgage loans instead of commercial loans.

Mr. LAVOIE: But there is a limit.

Mr. GRÉGOIRE: But allowing for this limit, and allowing for the time factor, it will still be an inducement for the banks.

Mr. LAVOIE: I hope there will be another review of the Bank Act in ten years.

Mr. LAFLAMME: May I put a supplementary question to Mr. Grégoire? There is this matter of making unlimited mortgage loans under this 10 percent. Is that not one of the areas where the forces of competition will have their greatest effect?

Mr. LAVOIE: Obviously, if we want to make mortgage loans, we will have to follow current market rates. If the market rate is  $7\frac{1}{2}$  or  $7\frac{3}{4}$  percent, we will not be able to make loans at 8 or  $8\frac{1}{4}$  percent, if we want to compete with other lending institutions.

The CHAIRMAN: What about—

Mr. GRÉGOIRE: 2 percent per annum. What is this 2 percent? What does this 2 percent mean in absolute terms? What is the amount?

Mr. LAVOIE: It depends on our Canadian deposits. 2 percent of Canadian deposits.

(English)

Mr. PATON: Perhaps, Mr. Grégoire, I could correct the record here. The limitation in amount on mortgage investment is solely in the residential conventional field. We understand that. There is no limitation in amount on our participation in N.H.A. mortgages; but there is a limitation on conventional residential.

(Translation)

Mr. GRÉGOIRE: But that maximum is  $6\frac{3}{4}$  per cent.

(English)

Mr. PATON: The limitation on conventional residential mortgages is 3 per cent for the first year which can be expanded 1 per cent per year so that within eight years a bank wishing to use the maximum availability under the act could reach 10 per cent of their Canadian dollar deposit liabilities plus outstanding bank debentures. That is the limitation as it currently stands in this Bill No. C-222.

(Translation)

Mr. GRÉGOIRE: What amount would this 3 percent mean in absolute terms? What would be the corresponding amount with respect to conventional mortgages?

(English)

Mr. PATON: It would be 3 per cent of our Canadian deposit liability today because we have no debentures—\$600 million Mr. Coleman says.

Mr. COLEMAN: Canadian dollar deposit liabilities are between \$19 and \$20 billions.

Mr. GRÉGOIRE: In August, 1965, \$19 billion.

The CHAIRMAN: It is a quarter after ten; does the Committee wish to continue?

An hon. MEMBER: Mr. Chairman, I have only one question.

The CHAIRMAN: We should ask Mr. Grégoire if he feels he is reaching the end of his questioning here.

Mr. GRÉGOIRE: Yes, I think in two minutes I will be finished.

(Translation)

But will this \$600 million be diverted from the commercial loan field to the conventional mortgage field? In other words, to find the \$600 million you need for mortgage loans, will the chartered banks have to reduce, by an equal amount, their commercial loans or personal loans?

(English)

Mr. PATON: No, sir. We have reiterated on more than one occasion here that we are completely conscious of our responsibility to our normal borrowers, our commercial borrowers and our personal borrowers. We would hopefully be able to attract additional resources which would enable us also to participate in a meaningful manner in this new form of lending under Bill No. C-222, but it would not mean that the attraction of a premium interest rate would be of such importance to us that it would be to the detriment of the normal recipients of our loans.

(Translation)

Mr. GRÉGOIRE: Now, at the present time, your loans are just about at a par with your deposits. Where will you find this additional \$600 million to lend out in the form of mortgage loans?

(English)

Mr. PATON: Mr. Grégoire, our loans are not balanced with our deposits. I think the deposit figures I quoted today were in the area of \$20 billion odd and for our general loans, I think, the figure I quoted was in the area of \$14 billion so it is a 14 x 20 ratio at the present time. Obviously the remainder of our deposits are in other assets: the liquidity assets have to be taken into consideration.

(Translation)

Mr. GRÉGOIRE: But you will have to take this \$600 million from other places. You will have to take that away from other investments, will you not?

(English)

Mr. PATON: We would, hopefully, attract whatever amount we put into this form of lending from other deposit gathering institutions,—we have mentioned this before—plus the issuance of debentures which will be quite an important adjunct to our ability to service this type of lending in the future.

(Translation)

The CHAIRMAN: Mr. Laflamme, you had one question, I believe?

(English)

Mr. LAFLAMME: I have just one brief question to Mr. Paton. Will you insure your conventional mortgage loans?

The CHAIRMAN: Do you mean life insurance?

Mr. LAFLAMME: Yes.

Mr. PATON: I would say, not as a policy matter, but there would be nothing to preclude a mortgagor from taking out mortgage insurance on his own behalf, as they do in many cases currently, Mr. Laflamme.

Mr. LAFLAMME: May I direct a question, then, to Mr. Elderkin. Is there anything in the proposed amendments, Mr. Elderkin, that prevents banks from insuring their conventional mortgage loans.

Mr. ELDERKIN: They cannot act as an insurer; they can require insurance.

Mr. LAFLAMME: Yes, but they will have the right as policy to establish insurance.

Mr. ELDERKIN: To require insurance.

Mr. LAFLAMME: They will have the right to require insurance.

Mr. ELDERKIN: Yes, but not to insure.

Mr. LAFLAMME: Not to insure themselves but to ask insurance companies to insure.

Mr. ELDERKIN: This, of course, Mr. Laflamme, is quite common in the personal loans.

Mr. LAFLAMME: Yes, indeed, I agree with that.

Mr. ELDERKIN: In many cases, indeed, the mortgagor would probably wish it because it would that mean if he died during the course of the term of the loan, why his loan would be paid off without any debt falling on the estate.

Mr. LAFLAMME: Would you then be inclined to follow the same policies as the N.H.A. regarding the rates of insurance—

Mr. ELDERKIN: That is a different type of insurance, Mr. Laflamme. That is insurance to the lender, if you will, and which is very common on the N.H.A. There are other types of insurance, too, on various debts to banks, where they may ask for life insurance which would pay off any debt due to the bank in case the borrower died during the term of the loan. As I said it is quite common in the personal loan field.

Mr. LAFLAMME: Thank you.



The CHAIRMAN: Have we completed our questioning at this stage on the area of mortgage lending by banks? Or are there others who have questions?

Some hon. MEMBERS: Agreed.

*(Translation)*

Mr. GRÉGOIRE: On the adjournment motion, I would like to ask for some information. We received the brief presented by a bank which we asked be not made public before next Tuesday. We were told that the Chairman of that bank would present this brief with regard to one of the subsidiary companies of the bank. Is this brief to be presented to us on Tuesday? Will that be the first item on the order of business next Tuesday, or next Thursday?

The CHAIRMAN: The Chairman of the Bankers' Association has just sent over a memo to me indicating that there would be some difficulty in obtaining the attendance of this witness.

It would be preferable, if the committee shares my view on the subject, to attempt to complete our questioning on the Bankers' brief before moving on to other witnesses representing individual banks. It is my intention to ask individual banks if it would be possible for them to delay until next Tuesday the attendance of the President. However, there are certain difficulties in the way. It has been indicated to me that the President of the Bank of Montreal and the President of the Royal Bank will have some difficulty in meeting with us next Tuesday. I think that it will not be possible to discuss these questions in plenary session. I will attempt to resolve the matter next Thursday with the assistance of the steering committee and in consultation with our witnesses representing the banking industry.

Mr. GRÉGOIRE: Could we be told before next Thursday?

The CHAIRMAN: Certainly.

Mr. GRÉGOIRE: I would be in favour of having the President of the Royal Bank here next Thursday, because we have had this brief. We could go on with the Bankers' Association after that.

The CHAIRMAN: If the situation changes, we could change our order of business, because after all, we make our own order of business. If he does not come Thursday, he will come a few days later. However, we will keep your suggestion in mind, and there will be an indication about that before next Thursday.

*(English)*

This meeting is adjourned until Thursday morning.







OFFICIAL REPORT OF MINUTES  
OF  
PROCEEDINGS AND EVIDENCE

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and/or a translation into English of the French.

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LÉON-J. RAYMOND,  
*The Clerk of the House.*

HOUSE OF COMMONS  
First Session—Twenty-seventh Parliament  
1966

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STANDING COMMITTEE  
ON  
**FINANCE, TRADE AND ECONOMIC AFFAIRS**

*Chairman:* Mr. HERB GRAY

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MINUTES OF PROCEEDINGS AND EVIDENCE  
No. 26

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THURSDAY, NOVEMBER 24, 1966

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Respecting

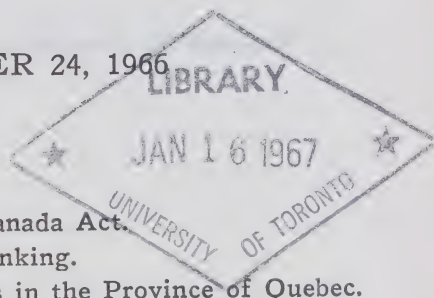
Bill C-190, An Act to amend the Bank of Canada Act.  
Bill C-222, An Act respecting Banks and Banking.  
Bill C-223, An Act respecting Savings Banks in the Province of Quebec.

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WITNESSES:

*From The Canadian Bankers' Association:* S. T. Paton, President; Leo Lavoie, Vice-President; J. H. Coleman, Vice-President; W. T. G. Hackett, Chairman of Canadian Bankers' Association Bank Act Revision Committee; G. R. Sharwood, Deputy Chief General Manager, Canadian Imperial Bank of Commerce; E. Cate, Q.C., Solicitor for The Canadian Bankers' Association; F. L. Rogers, Chairman, The Canadian Bankers' Association Economists Committee; B. W. Powers, General Manager (Administration), Bank of Montreal.  
*And also:* C. F. Elderkin, Inspector General of Banks; Denis Baribeau, Research Assistant.

ROGER DUHAMEL, F.R.S.C.  
QUEEN'S PRINTER AND CONTROLLER OF STATIONERY  
OTTAWA, 1966



STANDING COMMITTEE  
ON  
FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. Herb Gray  
*Vice-Chairman:* Mr. Ovide Laflamme  
and Messrs.

Addison,	Comtois,	*Leboe
Basford,	Flemming,	Lind,
Cameron ( <i>Nanaimo-</i>	Fulton,	McLean ( <i>Charlotte</i> ),
<i>Cowichan-The Isands</i> ),	Gilbert,	Monteith,
Cashin,	Irvine,	More ( <i>Regina City</i> ),
Chrétien,	Lambert,	Munro,
Clermont,	Lamontagne,	Valade,
Coates,	Langlois ( <i>Mégantic</i> ),	Wahn—(25).

Dorothy F. Ballantine,  
*Clerk of the Committee.*

\*Replaced Mr. Johnston at the afternoon sitting, November 24, 1966.



## ORDER OF REFERENCE

THURSDAY, November 24, 1966.

*Ordered*,—That the name of Mr. Leboe be substituted for that of Mr. Johnston on the Standing Committee on Finance, Trade and Economic Affairs.

Attest.

LÉON-J. RAYMOND,  
*The Clerk of the House of Commons.*



## MINUTES OF PROCEEDINGS

THURSDAY, November 24, 1966.  
(49)

The Standing Committee on Finance, Trade and Economic Affairs met at 11.10 a.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Addison, Chrétien, Clermont, Comtois, Flemming, Fulton, Gilbert, Gray, Johnston, Laflamme, Lambert, Latulippe, Lind—(13).

*Also present:* Mr. Thompson.

*In attendance:* Messrs. S. T. Paton, President, The Canadian Bankers' Association and Vice-President and Chief General Manager, The Toronto Dominion Bank; Leo Lavoie, Vice-President, The Canadian Bankers' Association and Vice-President and General Manager, La Banque Provinciale du Canada; J. H. Coleman, Vice-President, The Canadian Bankers' Association and Chief General Manager, The Royal Bank of Canada; W. T. G. Hackett, General Manager (Investments), Bank of Montreal and Chairman of Canadian Bankers' Association Bank Act Revision Committee; Gilles Mercure, Assistant General Manager, La Banque Provinciale du Canada; F. L. Rogers, Economic Adviser, The Bank of Nova Scotia and Chairman, Canadian Bankers' Association Economists Committee; G. R. Sharwood, Deputy Chief General Manager, Canadian Imperial Bank of Commerce; E. Cate, Q.C., Solicitor for the Canadian Bankers' Association; B. W. Powers, General Manager (Administration), Bank of Montreal; J. H. Perry, Executive Director, The Canadian Bankers' Association; C. F. Elderkin, Inspector General of Banks; and Miss M. R. Prentis, research assistant.

The Committee resumed consideration of the banking legislation.

On motion of Mr. Lambert, seconded by Mr. Laflamme,

*Resolved*,—That the following witnesses be heard on the dates named:

Tuesday, November 29

J. Douglas Gibson

Thursday, December 1

G. Arnold Hart, Chairman  
and President, Bank of Montreal

Tuesday, December 6

W. Earle McLaughlin,  
Chairman and President,  
The Royal Bank of Canada

Thursday, December 8

The Mercantile Bank of  
Canada



Messrs. Paton, Coleman and Hackett were questioned.

At 11.30 a.m. the Vice-Chairman took the Chair and at 12.30 p.m. the Chairman resumed the Chair.

At 1.00 p.m. the Committee adjourned until 3.45 p.m. this day.

#### AFTERNOON SITTING

(50)

The Committee resumed at 3.50 p.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Clermont, Fulton, Gilbert, Gray, Johnston, Lambert, Latulippe, Lind, Munro—(9).

*In attendance:* The same as at the morning sitting and Mr. Denis Baribeau, research assistant.

Messrs. Paton, Lavoie, Coleman and Elderkin answered questions put to them by the Committee.

Mr. Cate was called and questioned.

In answer to a question posed earlier, Mr. Baribeau tabled and explained a chart entitled *Number of New Housing Units Financed through NHA Mortgage Loans by Type of Lender and Areas for the Year 1959*.

*Agreed,* That the chart tabled by Mr. Baribeau be included in the Evidence. (*See Evidence*).

At 6.00 p.m. the Committee adjourned until 8.00 p.m. this day.

#### EVENING SITTING

(51)

The Committee resumed at 8.15 p.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Clermont, Fulton, Gilbert, Gray, Johnston, Latulippe, Lind.

*Also present:* Mr. Caouette.

*In attendance:* The same as at the morning sitting.

The Committee continued questioning of the witnesses and Messrs. Paton, Lavoie, Coleman, Sharwood, Rogers and Elderkin were questioned.

Mr. Powers was called and questioned.

The Committee having completed its questioning on the brief submitted by the Canadian Bankers' Association, the Chairman, on behalf of the Committee, thanked the Association's representatives for the assistance they had given the Committee.

Mr. Paton thanked the Committee for their co-operation and the manner in which the Association's representatives had been received.

The witnesses were discharged, subject to recall for further questioning.

At 10.05 p.m. the Committee adjourned until 11.00 a.m., Tuesday, November 29, 1966.

Dorothy F. Ballantine,  
*Clerk of the Committee.*





## EVIDENCE

*(Recorded by Electronic Apparatus)*

THURSDAY, November 24, 1966.

The CHAIRMAN: I call the meeting to order. Before we resume our questioning I should bring to the attention of the Committee a matter of scheduling. While the Committee, I think, should take into reasonable account the schedules of potential witnesses there are of course, limits beyond which the Committee can not go because of its own responsibilities. However, I do not think we have reached this point yet. But, I should explain why the Committee is proceeding now to try and complete the initial questioning of the Canadian Bankers Association. One obvious reason would be that it is more orderly not to interrupt this consideration to hear certain individual witnesses from the banking industry. But, the more direct reason is that our next two witnesses, as the Committee knows, are to be Mr. McLaughlin, President of the Royal Bank and Mr. Hart, President of the Bank of Montreal. It would appear that because of certain very important commitments great difficulties would be created if the Committee insisted on proceeding with these gentlemen either today or tomorrow or next Tuesday or next Thursday. I therefore would recommend to the Committee that we attempt to complete our major questioning of the Bankers Association in the hearings today, with a view to having Mr. Hart of the Bank of Montreal before us on Thursday, December 1, and Mr. McLaughlin on Tuesday, December 6, and the Mercantile Bank people on Thursday, December 8. They might take a little longer than the others.

Now, that leaves this coming Tuesday free and since I feel we should move along and use all time available to us for our work, I would like to recommend to the Committee that we reconsider a previous decision to hear Mr. Douglas Gibson, former President of the Bank of Nova Scotia along with other individual witnesses after we have completed with the people from the banking industry. The Committee may agree, on reconsideration, that he has a particular status even though he is not actually associated with the bankers, because of his previous experience and professional activity. The Committee may wish to reconsider its previous decision, in order to use the time available to us next Tuesday, most effectively, and authorize me to invite Mr. Gibson to present his brief, which I understand is quite comprehensive, on that day. Would someone be willing to make a motion to that effect? I ask for a motion because apparently at an earlier session the Committee had decided otherwise.

Mr. LAMBERT: I so move.

Mr. LAFLAMME: I second the motion.

The CHAIRMAN: Is there any discussion?

Mr. FULTON: Just before you put the question, because there is one thing implicit in what you said, namely, that we hoped to finish with the Bankers' Association today—

The CHAIRMAN: I deliberately used the term "major questioning". I was going to suggest to the Committee that the witnesses be excused with the understanding that we would reserve the right to recall them, after we had heard certain other witnesses, to deal with other matters arising out of other briefs or to give them an opportunity—

Mr. FULTON: I had in mind particularly that we have not yet seen the draft legislation on deposit insurance.

The CHAIRMAN: Yes, that is another reason why this should be implicit in any comments on my part that we try and complete the major questioning today, subject to your comment and what I have just said. Is there any further discussion on the motion? Are we agreed on the motion then?

Motion agreed to.

When we adjourned on Tuesday, we had just completed what I call our major questioning on the topic of mortgage lending. The next topic in the brief of the bankers is that of debenture financing. Do we have any further questions at this time on the topic of debenture financing? Mr. Thompson?

Mr. THOMPSON: My questions, Mr. Chairman, are really seeking information. I find that it is much easier to agree with this section than the previous one and probably the one before that. Therefore, if you will excuse me, Mr. Chairman, I am going to go over briefly what I interpret to be the procedure and perhaps you might check me, or add to my remarks as I make them.

Under clause 77, I think it is, the banks will now be authorized to borrow money on the issue of debentures for a term of five years not exceeding 50 per cent of the total paid up capital. Then, specifically, the debentures are not to be considered as deposit liabilities. They are not to be construed then as in any way cash reserves. Is that correct?

Mr. S. T. PATON (*President, The Canadian Bankers' Association*): No cash reserve would be required against them.

Mr. THOMPSON: No. Therefore, these debentures are subordinate to deposit liabilities, correct?

Mr. PATON: Correct, sir.

Mr. THOMPSON: The one point I am not quite sure about in this is the procedure to be followed in the issuance of debentures. The words "borrow money by the issue of debentures" indicate that the chartered banks cannot use the formula in 77(6); is that correct?

Mr. PATON: They must be issued under these subclauses, Mr. Thompson, yes.

Mr. THOMPSON: Am I right then in saying that banks must borrow before they can issue debentures or sell debentures to investors. Once this has been done the maximum amount of debentures they can issue is determined by the formula that is outlined here? Are we correct in that?

Mr. PATON: I am afraid I am not quite following your comments, Mr. Thompson. Do you mind repeating them?

Mr. THOMPSON: I am trying to get at the procedure that is to be used. Actually my question was this. Is it correct to say that the banks must borrow,

and I put that in quotes, before they can issue debentures or sell debentures to investors?

Mr. PATON: No, sir. The actual issuance or sale of debentures, in the same manner as any other securities are marketed, would initiate the transaction and the funds received from these sales would then come into the banks' position and be part of their liabilities. There is no question of them doing anything in advance of that to complete the required regulations under this section of the act.

Mr. THOMPSON: I was using that terminology only more or less as a quotation from the terminology that we have been using about it, necessarily having to borrow first in order to be able to sell. The terminology refers back to the terminology that you have been using or has been used here in the Committee on where the bank gets its assets from in order to pay for this transaction.

Mr. PATON: The bank is not getting an asset when it issues debentures. It is creating a liability.

Mr. THOMPSON: I realize that.

Mr. PATON: It is in effect borrowing through the medium of the sale of debentures to institutions and the investing public. That is right.

Mr. THOMPSON: I mention that because debentures do not require the reserve, as do normal loans; is that correct?

Mr. PATON: As do normal deposits, correct.

Mr. THOMPSON: Normal deposits. Nothing is said about the rate of interest in this regard. Is this to be determined without any—

Mr. PATON: This would be determined under the current market conditions if and when the issues were made.

Mr. THOMPSON: There is no limit to it?

Mr. PATON: There is no limit to it on either side other than the market dictates.

Mr. THOMPSON: I think that is the only question I have, Mr. Chairman. I would add that I think this is a very good addition to the act as well as the former point we were discussing that the banks move into the mortgage field.

The VICE-CHAIRMAN: Do you have a supplementary question, Mr. Gilbert?

Mr. GILBERT: Are you going to use investment institutions to issue your bond debentures or are you going to use one of the near banks?

Mr. PATON: I would assume these securities would be marketed in the normal manner for triple A risks. This would be a question for each individual bank to decide which vehicle they would use.

Mr. FULTON: Do you think there would be any conversion right attached to them?

Mr. PATON: Under this act, sir, there would not be.

The VICE-CHAIRMAN: Mr. Addison?

Mr. ADDISON: I have one point I would like to make. Under the arrangements in clause 77 banks will now be allowed to issue debentures, and one of the



reasons an organization such as RoyNat, for example, was created, was to provide term financing and also issue debentures on a longer term basis. The question I would like to ask Mr. Paton, now that the banks will be allowed to enter this field of debenture financing, do you still feel there is a need to have an organization such as RoyNat allied to a particular bank when, in fact, the bank can now do this itself?

Mr. PATON: Perhaps I could defer to Mr. Coleman in view of the fact that RoyNat is particularly mentioned, Mr. Addison.

Mr. FULTON: May I just make a point? Would it not be better to wait until we are on another section? There is a section on page 10 of the submission, limitation on bank participation in corporate ventures.

Mr. ADDISON: Well, the point of my question really is obviously, are the banks going into longer term financing now they can issue debentures where they could not before? If they are, then we will talk about the other on the other section.

Mr. J. H. COLEMAN (*Vice President, The Canadian Bankers' Association*): Well, Mr. Addison, I would say that mortgage lending is one form of long term lending the banks will definitely be going into. They will be borrowing long on debentures and lending long on mortgages. Would you like me to defer an answer to Mr. Addison's first question until we get to the other section or would you like me to answer it now?

The VICE-CHAIRMAN: I feel the question was properly put and I think you could answer now.

Mr. ADDISON: What I am really asking is if the banks are going to enter the same type of operation as an organization such as RoyNat, term financing for business enterprises?

Mr. COLEMAN: The banks will be able to do this. They will be able to take the security that is peculiar to long term financing, mortgage security, and so on, but when RoyNat was created there was, we felt, a definite void for an institution of this type. There are five corporate shareholders, a large capable staff which has been built up of engineers, accountants and lawyers and so on. Naturally, we would like to see RoyNat continue. We think there will continue to be lots of room for RoyNat to operate and from the standpoint of competition it is just one more institution competing for business and as a result the general public should be better off.

Mr. ADDISON: But the banks will now be allowed to participate in this type of business. In other words, there will be competition—

Mr. COLEMAN: Yes.

Mr. ADDISON: —by the banks in this form of financing?

Mr. COLEMAN: That is right but, Mr. Addison, I would doubt whether the traditional type of financing taken by chartered banks would change too much. The prime function of a bank is commercial lending and there has been very little long term lending apart from N.H.A. mortgages. Now there have been exceptions and of course if and when we are able to get into the residential mortgage business that will be long term lending. But, I would think that by far

the greatest percentage of chartered banks lending will be in the financing of receivables and inventory and day to day functions of the bank that have been prevalent in the banking industry since the inception of the banks.

Mr. ADDISON: But because of the ability now to borrow on debenture borrowing you will be able to enter into longer term financing, term financing.

Mr. COLEMAN: That is right but we could do that without debenture financing, too. It is certainly much easier to do it if you can borrow on a long term basis. But, the facility will be there for the banks to do that.

Mr. PATON: I might add to that, perhaps, Mr. Addison. Under subsection 6 of the act the total amount in the first year if used to its maximum, will be roughly in the neighbourhood of \$125 million for the whole banking system.

Mr. COLEMAN: Mr. Chairman, I think that is residential only, though.

Mr. PATON: I am speaking of debentures.

Mr. COLEMAN: Oh, yes; I am sorry.

Mr. PATON: The 50 per cent that Mr. Thompson referred to can be reached over a period of five years. It is 10 per cent, per year, of capital and rest account.

The VICE-CHAIRMAN: Do you have other questions, Mr. Addison?

Mr. ADDISON: No, fine, thank you.

(Translation)

Mr. CLERMONT: My question is for Mr. Lavoie. The bank will be issuing non-guaranteed debentures. Is this up to 50 per cent?

Mr. LAVOIE: Mr. Clermont—

Mr. CLERMONT: To make up to 50 per cent at once or so much per year?

Mr. LAVOIE: For the financial year of 1967 the authorized sum is 10 per cent, capital and bank reserves. But this increases each year by 10 per cent, up to 50 per cent.

Mr. CLERMONT: Fifty per cent is the maximum allowed amount?

Mr. LAVOIE: Yes, that is the case.

Mr. CLERMONT: What is the initial sum of the debenture, \$100. or what?

Mr. LAVOIE: You mean the amount of each debenture issued on the market? I think it will be left to each bank to decide.

Mr. CLERMONT: But under the present bill, it is to be left to the discretion of each bank, is that the case?

Mr. LAVOIE: Yes.

(English)

The VICE-CHAIRMAN: Does anyone have other questions on that topic? Then I think we will move on to the topic of changes in reserve requirements, at page 70. Mr. Fulton?

Mr. FULTON: I had asked a number of questions with regard to reserves on an earlier occasion. It is not easy to recall just where we were at that moment, when we went back to the interest rate ceiling. But, as I recall it, Mr. Hackett

was giving evidence and answering on the basis of his experience with respect to this matter of the new requirement that the reserves be maintained and adjusted, as it were, on a bi-monthly basis. As I recall, I had just asked, or was leading up to a question I intended to ask, whether in your view it would be more acceptable to have this bi-monthly basis if you were allowed for the current two-week period to maintain a reserve on deposit on the basis of what should have been there on the last two-week period? So that instead of being penalized in this very short time for calculations now of two weeks, if you make a slight error, you would be allowed, in fact, to adjust on the basis of the experience of an immediately past two-week period. Do I make myself clear?

Mr. HACKETT (*General Manager (Investments), Bank of Montreal, and Chairman of Canadian Bankers Association Bank Act Revision Committee*): I think so, Mr. Fulton. If I understand you correctly, your suggestion would be that any overage or underage in the first two-week period could be carried forward into the second two-week period. Have I your question correctly?

Mr. FULTON: Yes.

Mr. HACKETT: Well, the only observation I can make as to that would be that I think that would, essentially, bring us back to where we are now, where we average over the entire one-month period, which we would consider to be a preferable method of arriving at the objective that both the Bank of Canada and the chartered banks are seeking. I am bound to say that I do not see any very substantial difference between that procedure and a full one-month averaging period, because what happens now is that if you run a bit ahead or a bit behind in the first two-week period you make it up in the second two-week period.

Now, I think the point we have been endeavouring to make here is that I am sure it would be the basis of the experience of people in the banks who are directly and daily concerned with this matter a two-week averaging period does not really give you time to deal in a smooth way with the kind of variations that you know are going to occur during the month. This is by and large a difference of view. The view of the banks who have to deal with this area and who have to work in it does diverge from the view of the central bank. I would like to emphasize again, there is no difference of opinion as to the objective.

There is, perhaps, one point I should add here which I think arises out of your question, albeit perhaps indirectly. We really will know how this thing works only when it is in operation. The banks have what we consider to be strong, good, practical reasons for doubting whether this will work the way the central bank hopes it will. We would even go further, and as we endeavoured to set out in the memorandum that has been tabled before the Committee, to give our reasons why we think the result may be even perverse. It will aggravate the difficulty, if there be a difficulty that the central bank is endeavouring to overcome.

Mr. FULTON: If I recall correctly, you said that if you narrow down to this two-week period, and you are going to pay a penalty if you are under, it may force you to make a more violent adjustment to avoid that than if you have a month to average.

Mr. HACKETT: That is indeed a major part of our case. Another part is that it would thereby conduce to perhaps an uneconomical use of cash. Having the



shorter period facing you, you can take less chance; you are almost bound to play the thing a bit more on the safe side and carry more cash than you would otherwise use, of, alternatively, we will probably be forced to hand a shock to the money market that we would not have to hand to it had we the full month's period to work out in.

Now, if I might finish the point I was leading up to in my reply, I think it would be this: It seems to us in an area where there is a legitimate area of doubt as to how this thing is really going to work out, what you gentlemen are being asked to do is to put this requirement in rigid legislative form for the next ten years. If it does not work the way the central bank thinks it will and if it does work the way we think it will, then we are hung with it for ten years and no one will be very happy about the outcome. That is a matter, as I said before, that goes a bit beyond the chartered banks and their response to central bank policy; it could also create unnecessary and unwarranted variations in the effect of chartered banks operations on the money market and vice versa.

Mr. FULTON: You said you felt if it was put on a two-week basis, with an adjustment to take account of any discrepancy in the previous two-week period, that in effect you would be having the situation you now have when it is a monthly calculation. I do not quite appreciate why you say that because it seems to me that you would have, on a two-week basis, adjustable on the basis of the previous two-week experience, that degree of flexibility of fairly rapid following of movements which the Bank of Canada is concerned about, as I understand it, but you would be avoiding the penalty. It seems to me you would be avoiding two things; one, the danger of having to pay a penalty and second the requirement of making a violent move in the money market to avoid a penalty. But would you not, in fact, have a slightly more flexible, or rapid following, of what the Bank of Canada is trying to get at, while at the same time avoiding penalties?

Mr. HACKETT: Mr. Fulton, I would hesitate to give an answer to that, as it were, off the top of my head. I think I would want to sit down with other people in this area and try to consider what the practical consequences might be. But, may I put it another way and I think perhaps we arrive at the same goal by a slightly different route.

I would like to go back to the point I made at the outset that there is no difference of view between the chartered banks and the central bank as to the desirability of each individual bank—because this is a matter for individual banks, the banks as a whole do not respond. The response is a result of decisions taken in eight individual banks daily. We appreciate that it helps the Bank of Canada. It smoothes the processes of monetary control if each bank responds as quickly and as precisely as it can to changes in its cash base brought about through the daily clearing system. In those responses we have to take cognizance of what has gone before and what we think is going to face us in the near future.

I am quite sure—indeed, I have often said to myself and said to my colleagues—that there must be times when the response of a chartered bank to the change in its cash base on any one day must be puzzling to the central bank. But it may not at all be puzzling to the bank itself, to the chartered bank concerned, because it may know of something that is going to happen tomorrow that the central bank is not aware of, or it may expect that something is going to

happen tomorrow and may not even know. But, it has to prepare in the light of that expectation.

Coming back to your question, sir—this I might say is a personal view although I suspect it is one that would be shared—my personal view would be that the better way to approach this problem would be to leave the averaging period as it is and for the chartered banks collectively or individually to say to the central bank: We will do our level best to operate as closely as we can on a basis whereby we would, as closely as we can, provided we can do so without handing unnecessary shocks to the market, try to average out in practice on a two-week basis. But, the minute you put that in rigid legislative form, then I think you create a lot of problems that are unnecessary problems.

Mr. FULTON: I agree that from your point of view it would be better if it were done on a voluntary basis but I am concerned with the practical—with what it may be sensible to expect—rather than what may be most desirable from your point of view. I would appreciate—and I would hope it is not putting you in a strait-jacket but I would like to put it this way—as clear an answer as you can give to me to this question. Assume that it is going to be a legislative requirement and the legislation is now going to be on a two-weekly or twice-monthly basis instead of once monthly. Would you be prepared to accept that, or would you find it acceptable, if you were allowed to make adjustments in the current two-week period on the basis of the previous two-weeks experience? What I mean is at the close off of the 15th of the month if it is found that you are a fraction below what should have been your maintained reserves during that completed period, that you then bring it up, by putting in the deficiency during the current two-week period, but without penalty. So, my question is—assuming you will be required to do it on a twice-monthly basis—would that not be a more acceptable and, in fact, less damaging requirement from your point of view?

Mr. HACKETT: Mr. Fulton, I may have to make a qualification here. I am sorry, but, this is a matter where there might be practical difficulties. But, let me say that on the basis you have stated to me, any additional flexibility, if we have to be put in this two weeks—I believe you used the words strait-jacket which I think is an adequate description—any measure of workable flexibility would, I think, be very acceptable. It would not, in my opinion, be a sufficient substitute for the basis under which we are operating now and which, I would add, for the system as a whole, appears to work remarkably well, having regard to the uncertainties that each bank must have to face every day.

Mr. FULTON: Perhaps I could put it this way, what you are saying then is that you prefer it to be left as it is now?

Mr. HACKETT: Correct.

Mr. FULTON: But if you are going to have to go to a bi-monthly or two-weekly basis you prefer it on the basis I have outlined rather than what is in the proposed bill? Is that what you are telling me?

Mr. HACKETT: Yes; I would agree with that. May I add one thing though, and I would like to underline that it is an honest and considered opinion that the procedure under which we now operate will work better from the standpoint of the system and from the standpoint of the central bank itself.



Mr. FULTON: Thank you. Perhaps I could ask some other questions about these changes in reserve requirements. When Mr. Rasminsky was before us I asked him whether in fact this split ratio of 4 per cent for notice deposits and 12 per cent for demand deposits would not bear unequally on the various banks, and most heavily on those supporting to the greatest extent the small businessmen, that is, any bank which concentrates, in its customers, on small businesses, whose deposits are in the demand category. Perhaps Mr. Paton would prefer to answer this one. If you have to maintain 12 per cent reserve for demand deposits—. Perhaps I should deal with this matter by two questions. First, is it a fact that in your experience the demand deposit is the type maintained by small business?

Mr. PATON: Perhaps Mr. Hackett might answer that initially Mr. Fulton.

Mr. HACKETT: I would answer the question in two parts, sir. The first would be that there undoubtedly is a variation at any one time between the percentage of demand deposits to total deposits of individual banks. It is not a major variation but it is significant. There will also be in any one bank, at different times, a variation in the ratio of demand to total deposits. Now that is part one.

Part two of your question, as I recall it, was, if the bank is a high loaning bank really is it likely to have relatively more demand deposits than a bank without such a high loan ratio? I think, and Mr. Paton may, indeed, want to add to this, it might be so. I think it would be difficult to substantiate at all times and under all conditions; the conclusion does not leap readily to the eye.

Mr. PATON: I would support that, Mr. Fulton. I think the relative relationship between the banks when associated with the type of business they are doing would not have a material effect on the demand deposits each bank holds by virtue of the business they handle. These deposits do fluctuate during the month and represent the funds that corporations and business people generally need in their day to day operations. I do not think legislation such as we are currently discussing would weigh in an undue manner on one bank versus another.

Mr. FULTON: If we had any tendency to discourage banks, or perhaps I could put it this way; encourage banks to concentrate on the type of business or the type of customer who maintains notice deposits rather than demand deposits—you have to maintain 12 per cent ratio for one and 4 per cent for the other—what do you anticipate would be the effect, if any?

Mr. PATON: Obviously on that basis notice deposits would be more attractive to a bank when the cash reserve is at a lower figure and there will be certainly enabling powers to us to be more competitive on notice deposits with a reserve of 4 per cent. One would expect possibly a change in the mix of deposits. Demand deposits, these days, are more truly the day to day working funds of the business community to a much greater extent than they formerly were. In the not too distant past corporate treasurers held quite substantial free funds with the banks on a non-interest basis, but in the last decade—possibly in an increasing extent since the money market become a viable instrument in Canada—corporate treasurers in turn have become much more conscious of the funds at their disposal and are taking them out of the demand category and putting them in the market in short term instruments. Notice deposits, of course, do carry interest and demand deposits do not. There is an expense to the bank in attracting notice



deposits but the reduction in the reserves is a very acceptable feature to the chartered banks.

Mr. FULTON: Yes. Is there any experience that you are aware of that to your mind demands this sharp distinction now to be made in the ratio of reserves maintained as between the two types of deposits? Or, would it not be—I will follow that question with another one which perhaps I should ask later but will indicate now so you know what I am getting at—in your judgment, on the basis of experience, would it not be equally safe and a lot simpler to require simply an average over-all for all types of deposits? So my first question is, is there anything in your experience which seems to indicate why this differentiation should be made? Then, I will come to my second question.

Mr. PATON: Would you like to respond to that, Mr. Hackett?

Mr. HACKETT: Mr. Fulton, I think that the institution of the lower reserve ratio on notice deposits is logical in itself and was also a logical follow-through with respect to the recommendations of the royal commission. With regard to the second part of your question, we find it difficult to rationalize the procedure whereby the reserve ratio against the demand deposits is raised to as high a level as 12 per cent. This would exacerbate this problem which you have already explored. In the case of an individual bank some sudden shift from demand to notice deposits could have quite an abrupt effect on the over-all reserve that that bank would be required to carry.

Mr. FULTON: Since you now have the proposed statutory requirement for secondary reserves, would it not, with respect to primary reserves, be more simple and more equitable simply to reduce the existing ratio from 8 per cent, say, to 6 per cent over-all?

Mr. HACKETT: I think the 4 per cent reserve against notice deposits does have a value in itself, in that it would, I think, make it easier for banks to develop new, possibly more attractive, different deposit media. I regard that as something that is good in itself without relationship to the ratio required against demand deposits. I would rather think—and I do not know to what degree there would be unanimity on this—the 4 per cent ratio against notice deposits which does recognize the desirability of flexibility and development of attractive deposit media combined with a lower ratio against demand deposits, would be perhaps more acceptable than the over-all average. I do not know whether Mr. Paton would care to add to that.

Mr. PATON: I think, perhaps, in summary we might say that the banks were in accord with the Porter Commission recommendation, Mr. Fulton, which as I recall it, was 8 per cent for demand, 4 per cent up to 100 days and nil over 100 days.

Mr. FULTON: Do you consider the sharp division, 4 per cent in one and right up to 12 per cent on the other is—the differentiation in rates—unduly sharp?

Mr. PATON: I think the answer to that would be yes, we would prefer a closer differential.

Mr. FULTON: I then come to the other question which is the only other one I want to ask on this section. It is about interest on your deposits. I appreciate the Bank of Canada Act does not allow, at the moment, for the payment of interest,

that is, interest on your reserves maintained with the Bank of Canada. So, it would require a change in the Bank of Canada Act, and I think you refer in your submission to your feeling that there should be some permissive authority given to the Bank of Canada to pay interest. In seeking to arrive at an understanding of the situation may I ask these questions. Whether the Bank of Canada Act required it or not you would have to maintain reserves to protect your liabilities?

Mr. HACKETT: Every bank, sir, would undoubtedly have to maintain a cash reserve.

Mr. FULTON: Yes. So the maintenance of a cash reserve has nothing to do with control of fiscal monetary policy. Perhaps that is an oversimplification. What I mean is that, even if the Bank of Canada were not an instrument through which control of monetary policy is exercised, even if it was not performing that function, but simply acting as the depository of reserves, you would still be required and would want to maintain reserves with it?

Mr. HACKETT: In the context of your question, sir, every bank would have to maintain a cash reserve. Now, the level of that cash reserve would not necessarily be the same for each bank and each bank would have the daily management decision of deciding what in its context was an adequate cash reserve and that decision would have to be made in relation, of course, to the level of their deposit liabilities, what clearing gains or losses the bank anticipated and in addition, and this is a very important addition, that cash reserve would also have to be appraised in the light of what other assets the bank had which were of a near cash nature, which could be readily converted into cash. But, I do not think it follows at all that the cash reserves would necessarily be the same for each bank or that they would be as high as the statutory requirements for each bank.

Mr. FULTON: Right. I would not think it would be practical to have a different reserve for each. You must have some statutory authority or statutory limit, so let us assume for the sake of argument at the moment, anyway, that it would not be practical to have a different level for each bank and that the exigencies of administration require a uniform level. I asked that original question because I want to go on to the question of secondary reserves and discuss the question of payment of interest on that. The point I am trying to make is that it seems, to me at any rate, difficult to justify a requirement or request that the Bank of Canada pay interest on the primary reserves since you have to maintain primary reserves anyway whether they are with the Bank of Canada or in your own institutions—

Mr. HACKETT: My comment on that would be that to the extent that a bank or the banks, if you wish to speak of them collectively, carry cash reserves with the Bank of Canada higher than would be necessary for day to day operating purposes, then, to that extent, we are supplying funds interest-free to someone. I am not too sure it is the Bank of Canada or the federal government; ultimately it is probably the federal government since the bank of Canada's profits are transferred to the Receiver General, and to the extent that we are by statute required to carry cash reserves higher than we would carry for ordinary working purposes, then I suggest that the non-receipt of interest on the excess is a form of additional tax—

Mr. FULTON: Yes.

Mr. HACKETT: —on banks, and I might add, a form of discrimination as between banks and near banks.

Mr. FULTON: Does this not become particularly apt, however, when you think of the secondary reserve you may be required to maintain, as I appreciate it, has really, if not nothing to do, then much less to do with the question of liquidity of a bank and much more to do with the control over monetary policy. In other words, am I right in assuming that the primary purpose for the Bank of Canada calling up the secondary reserves would be to make some adjustment as they see necessary in the state of the money market or the allowable extent of credit?

Mr. HACKETT: I think you are right.

Mr. FULTON: Then, although this is an acceptable and accepted function of the Bank of Canada, nevertheless to the extent that it is an obligation imposed on the Banks as a Bank of Canada requirement, is this the field in which you feel the Bank of Canada should pay interest to the chartered banks when they require this kind of reserve to be maintained?

Mr. HACKETT: Well, Mr. Fulton, the secondary reserve as arbitrarily defined for the purpose of this legislation, comprises three constituents. The first constituent which is the minor end of it is excess cash, that is, the cash you might have in a month over and above the minimum reserve requirement. If there is any excess, that goes into secondary. That would be the minor end of it. The two more major constituents would be government of Canada treasury bills which do bear interest at market rates and the day to day loans to the money market which also bear interest.

Now, under normal times, the interest on day to day loans which is a very volatile rate, it fluctuates not only day by day but through the day, and the interest on government of Canada treasury bills, would be at the very low end of the interest rate spectrum. They usually are at the low end but absolutely these rates vary from time to time depending on the interest cycle at the time. These are not sterile assets, day to day loans and treasury bills, from the standpoint of interest but they are low yielding assets. Now, to the extent that by reason of these requirements a bank carries more of its short term assets in this particular form, then to that extent such a bank is forced into carrying a less productive asset mix than would otherwise be the case.

I would like, if I may, as a supplementary answer to this question, to make another point which I think is quite important. As the association said in its brief to the Porter Commission, these secondary reserves are not in a true sense a reserve since they are not available for use. They are rather a forced investment. Now, in addition to maintaining secondary reserves that you have to keep, any bank in the ordinary course of its activities is going to have to put on top of that some secondary reserves of a short term nature. It may not be exactly the reserves as defined here but they will have to have some secondary reserves which they can use. Therefore, when you put what you would want to have on top of what you must have, which are frozen to all intents and purposes, the element of forced investment becomes rather more important and rather more obvious.

Mr. FULTON: Which part of the—

The VICE-CHAIRMAN: Mr. Fulton, I am sorry to interrupt you but I think your 20 minutes of questioning expired a while ago. I permitted you to go on



because your questions were in general terms that were of interest to all the members of the committee but unless I receive agreement from members of the Committee I will have to ask you to make this your last question and then I will pass to someone else.

Mr. FULTON: Yes, I think this will be my last question. On which part of the reserves maintained at the Bank of Canada are the banks asking for interest?

Mr. HACKETT: I will have to refer to the brief for one moment to get the information.

Mr. PATON: The answer, Mr. Fulton, is the cash reserves carried with the Bank of Canada.

Mr. FULTON: All of them?

Mr. PATON: The secondary reserves are not carried with the Bank of Canada; they are invested in securities. The funds we carry with the Bank of Canada on which no interest is paid is our primary reserve and that is the area in which we would suggest consideration be given to paying interest.

Mr. FULTON: On the whole of that primary reserve, or on part of it above a certain level; or have you given consideration to that aspect?

Mr. PATON: We have given study to that since the first round of questioning. I think you referred to this early in the hearings. As an approximate estimate I mentioned, off the top of my head—this was possibly a reasonably bald statement, although not as bald as Mr. Hackett's, a figure of 5 per cent and I was advised I had gone a little high with that. I think this is the area in which you would like some ideas. What would we normally consider we would need to look after our day to day clearing obligations and till money positions. Is that the area in which your question was asked?

Mr. FULTON: Yes.

Mr. PATON: I am not sure if we could put a figure on that. I think we could arrive at one if there was an opportunity to negotiate and see in what area we would like to put a request more specifically than we have to date. Would that be—

Mr. HACKETT: Yes, I think, Mr. Chairman, that what we are really after here is an area of reasonable negotiation. I think what we are after now is a point of principle rather than putting an actual figure forward.

Mr. FULTON: Thank you, Mr. Chairman.

The CHAIRMAN: I will now recognize Mr. Clermont, followed by Mr. Lambert and Mr. Lind.

Mr. CLERMONT: Mr. Chairman, are we only on reserves that the chartered banks have with the Bank of Canada or are we on general reserves?

The CHAIRMAN: I think it would be in order for you to discuss the question of reserves generally because I would say they are related to the context of reserves with the Bank of Canada. Aside from that, the question of reserves generally seems to be dealt with by the topic raised by the witnesses. Perhaps you should ask your questions and then it would be easier to define what you have in mind.

Mr. CLERMONT: I have in mind asking questions about inner reserves?

The CHAIRMAN: This is a topic that comes along later, specifically, in the brief.

Mr. CLERMONT: But right now it is only about reserves that the chartered banks have with the Bank of Canada? If that is the case, I will pass.

The CHAIRMAN: The inner reserves are a separate topic and we will be coming to that shortly. Mr. Lambert?

Mr. LAMBERT: Mr. Chairman, it would be my assumption that the Bank of Canada did not come to this decision about the two-week averaging and other requirements about secondary reserves on an overnight basis. I am wondering, when did the chartered banks become aware of the likelihood that the Bank of Canada would be making these requests and on what basis they advanced their arguments. What were the conditions, if you know what they were, which led up to this decision? What difficulties have existed in, shall we say, fiscal and monetary policy control, which would lead them to this. I know this could be answered also by the Bank of Canada but I would like to know from the banks' point of view when they became aware of this. Obviously, they have had discussions with the Bank of Canada officials in this regard.

Mr. PATON: Perhaps I could initiate the answer to that, Mr. Lambert and Mr. Hackett could supplement it. I think the correct answer to your question is that the first intimation we had that the secondary reserve would become statutory and that the variable reserve on different types of deposits would come into existence was when Bill No. C-222 received its first reading. To my knowledge, there was no prior official discussions with the bankers as a group.

Mr. Perry interjects that the proposed fortnightly averaging did come up, when the governor appeared before the Porter Commission. But, in so far as the actual inclusion in this act is concerned, this came without specific prior discussion with the bankers.

Mr. LAMBERT: Perhaps Mr. Hackett, who is concerned with the investment side of the bank would be able to add some information in this regard. Did they run into any difficulties, shall we say, with the Bank of Canada, with regard to the monthly averaging, so that there would be some concern by the Bank of Canada as to some of the effects of the monthly averaging.

Mr. HACKETT: Mr. Lambert, you will, of course, appreciate that I am now put in the position of giving hearsay evidence. But, this matter has been discussed both formally and informally with the Bank of Canada by the banks. I am sure that the Bank of Canada would be very well prepared to give its views on this matter. There has been an exchange of view, and at the risk of repetition I would like to say again there is no difference of opinion as to the objective the Bank of Canada is seeking. If I may say so, and if I am wrong I am sure that the Bank of Canada will correct the record if and when they wish to speak on this matter, I think the thing that bothers the Bank of Canada is this: on occasions, from where they sit—it is a little bit like the man who can walk around a bridge table and watch all four hands being played—from where they sit, they may see that some individual bank is, from their point of view, sitting on or potting up what looks like, from the outside looking in, an unreasonably high cash ratio for one, two, three or four days or conversely an unreasonably low cash ratio. Now that, and I need not go into the mechanics of it, undue or what appears to be an undue

concentration of cash at any point of the banking system, let us face it, I think it does to that extent complicate the operation of Bank of Canada technique from the standpoint of the exact amount of expansion or contraction they are trying to bring about on that particular day.

Now, to this I think the banks would have two answers. One is that if you sat where the bank concerned sits, there may have been a very good reason for what looks like a temporarily eccentric cash behaviour. That bank is anticipating something or it may even know something. I would say that more often it is a matter of anticipation because there is a great deal of guesswork in this operation. By holding its fire, as it were, by not reacting at that moment of time, the bank in so doing may, in fact, be forestalling a much more abrupt adjustment three or four days afterwards. But, at that moment and from the standpoint of the central bank it may create a problem.

Now, the second point we would make and which we have made is this: Every bank in running its cash, and the swings are extremely volatile, has to prepare for uncertainty. It is trying, each bank is certainly trying, to run that cash ratio as fine as it can. No bank wishes to see unused cash piling up for any length of time. Nothing wrings a banker's heart more than seeing cash which is not working. You are continually guessing in this area. If you guess wrong you are fined. If you guess wrong in the sense of having less cash than you required. If you guess wrong in the sense of having more cash than you require you are fining yourself because you are leaving cash unemployed. Now the second point we will make here is really this. Under the proposed two-week system the uncertainties are going to be there just the same. Nothing will happen to eliminate these uncertainties, to eliminate these swings, but mathematically the impact of X number of dollars by way of a swing will be doubled in terms of our requirement to meet this cash ratio. Therefore, it may well be that faced with some cash loss this matter of what looks like temporary eccentric behaviour on the part of individual banks will not be lessened. The problem will, if anything, be aggravated.

Mr. LAMBERT: Well, Mr. Paton, this information likely has been given but not having the transcript available, could you tell me about how much coinage the banks hold because you do make this proposal that within your cash reserves there be counted the coinage.

Mr. PATON: The figure, quoted previously, was \$40 million. That is approximately correct, Mr. Lambert.

Mr. LAMBERT: I see, and if this were included what percentage of the cash would you consider this to be?

Mr. PATON: I think the figures we quoted the other day were that the average holdings of Bank of Canada notes was in the area of \$465 million. Is that exclusive of silver?

Mr. HACKETT: The cash reserves, the Bank of Canada notes, the till money held by the chartered banks is of the order of \$470 million. The silver in relation to notes would be roughly ten to one.

Mr. LAMBERT: If the coin were counted in, what percentage effect do you think this would have on, shall we say, your provision of reserves.

Mr. PATON: The average daily deposits carried by the chartered banks were \$965 million last year to which—



Mr. HACKETT: It was \$960 million and about \$450 million of notes. That is about the ratio.

Mr. LAMBERT: What I am trying to get at is, if the coinage was to be included as requested is it a significant item or is it a relatively insignificant item?

Mr. PATON: It is significant, Mr. Lambert; relatively in relation to the total it, perhaps, is not of major importance but it is, in effect, \$40 million of free assets we are carrying on behalf of the governing authorities on which we receive no interest. If the \$40 million were included and we were able to release or free that much into earning assets, it would be of material benefit to the banks.

Mr. LAMBERT: Going to the point that Mr. Fulton was discussing about the difference in the reserve requirements for demand deposits as against notice deposits, would the wide differential that is now proposed not have the effect of tending to standardize banking operations, putting in a greater degree of uniformity between the various banks. It was indicated that, shall we say, the high loaning bank because of this very high differential might be driven to a much more uniform mix with its competitors. In other words, there is a disincentive as a result of this 8 per cent difference for a bank, shall we say, to specialize in commercial loans and high lending as against taking on more term deposits.

Mr. HACKETT: I do not think, Mr. Lambert, we did establish that there was a very clear correlation between the deposit mix as against demand and notice deposits and loan ratio. I think, if I recall, I said myself that the correlation does not leap to the eye. I think it might possibly—let me say it this way. If any bank found that its deposit mix was chronically putting itself at something of a disadvantage vis-à-vis other banks, then it would certainly be under incentive to make some kind of a change in its assets, although, I do not quite know what that change might be. But it would be under some incentive to make some adjusting change on the asset side to make up for the chronic disability it may have been suffering as a result of a high proportion of high reserve attracting deposits.

Mr. LAMBERT: This is the point I am turning over in my mind, that this distinction between the two classes of reserves that are being established under this legislation may tend to constrain the banks in their freedom to operate and, therefore, be less competitive. This may be one of the negative aspects of, shall we say, the two-rate structure, particularly if there is a wide gap. Certainly it would not be so much of a disincentive if the rates were 8 and 4 as against 12 and 4.

Mr. HACKETT: We are certainly going to be doing a new set of sums. It is something we are all going to be very conscious of.

Mr. LAMBERT: Well, it has been suggested to me to put it another way. Might not this be a disincentive to really carry on a very heavy current account business?

Mr. FULTON: Every current account is a demand deposit, is it not?

Mr. LAMBERT: And against which you must put 12 per cent on which you are not earning interest, whereas, I know that even though you are only paying 4 per cent or have to put up 4 per cent on term deposits, and these cost you

money, yet because of that 8 per cent gap or differential, there will be in actual fact a disincentive to carry accounts, or specialize in, the current deposit field?

Mr. PATON: I think we must remember Mr. Lambert in the acquisition of demand deposits that these do not receive interest which would offset the disadvantage of providing the substantially greater cash reserves. This would be an incentive rather than a disincentive looking at it from that angle. I think in general we would, and we have already gone on record that we would, be happy with a split ratio. We would prefer to have the 12 per cent at a lesser rate. As you are well aware, under the present act the primary cash reserve we are currently operating under for all deposits has a variable factor. Under the present legislation the Bank of Canada has statutory powers to increase that at certain stated intervals. This power has not been used in recent years of banking. But, there is that variable provision in the existing legislation with regard to the primary reserve. Under the proposed bill we are now looking at, this variable provision is eliminated from the primary reserve and, indeed, transferred over to the secondary reserve.

The CHAIRMAN: Do you have a supplementary question, Mr. Fulton?

Mr. FULTON: I am afraid I do not follow what Mr. Paton said about a variable provision. If you are speaking about the differential in the reserve which must be maintained as against notice deposits and term deposits, that surely is with respect to the primary reserve and not with respect to the secondary reserve?

Mr. PATON: I was speaking of the act we are currently operating under.

Mr. FULTON: Yes. But you said under the new proposed act this is taken out of the primary reserve and carried into the secondary reserve.

Mr. PATON: Under the new act there is a fixed ratio of 12 per cent on demand deposits.

Mr. FULTON: Yes.

Mr. PATON: It is fixed and will not be adjusted during the oncoming ten years.

Mr. FULTON: I see now. I had misinterpreted the effect of your explanation.

Mr. LAMBERT: The last area of my questioning, Mr. Chairman, concerns the instrument of the reserves being used by the Bank of Canada for fiscal and monetary control, that that portion above what the banks would themselves carry, that slice above it to the point now of 8 per cent, is the instrument of fiscal and monetary control by the Bank of Canada. If you were to get interest on this portion the result would be to diminish the extent of the effectiveness of this instrument and I am being, shall we say, the devil's advocate here, in regard to the idea of the primary and secondary reserves without interest. They really become much more effective without an interest earning capacity.

Mr. HACKETT: Well, Mr. Lambert, we are moving into a somewhat different area now, the area of monetary control. The only useful observation I might be able to make on that is, from the standpoint of monetary control I should not myself have thought it mattered very much what the absolute ration requirement was. I think an economist could make a very good case that a central bank

could operate monetary control very well with almost any kind of a cash ratio because it always has the power and exercises the power to make cash plentiful or scarce in relation to that target.

Now, I would agree with you that if a banker sits and pots up cash, then to that extent the effectiveness of monetary control might be impaired but I look at this thing myself in somewhat three layers, as it were which is the kind of thinking you have to do if you were attempting to work out a formula for this thing. There is the cash that a bank would have to keep anyhow. That is layer one. Sorry, let me rephrase my statement there. There is the cash that a bank would keep voluntarily for the ordinary purposes of its operations, for meeting its clearing balances. On top of that layer there is a second layer which is the difference between what it would wish to keep and what legislation says it must keep. Now, it is in that area, I suggest, that there should be some interest remuneration to the banks. Then you could look at a third and much smaller layer which comes on the top of the first two which would be excess over this statutory figure. It is only when you get there that I think the point you make of this excess perhaps impairing the processes of monetary control begins to be valid. Now, that is a very small area. It is a very small excess and I think these three elements would have to be taken into consideration in attempting to work out some kind of a formula. I do not think the point you make in the context of the way the principle could be applied would be a major point, sir. In fact, I am not at all sure that it would even be a point if the formula were adjusted to take this into account.

Mr. LAMBERT: Is it also a point that to the extent that the central bank exercises monetary control by increasing the reserve requirements, shall we say, from the primary reserves into the secondary reserves that since the secondary reserves would not be earning interest nor what you call the second layer, that the exercise of monetary control bears upon the bank's loan in so far as cost is concerned.

Mr. HACKETT: The greater part, sir, of the secondary reserves do earn interest. They are day to day loans to the money market and treasury. But the Bank of Canada does not pay us that interest. In the case of day to day loans, money market dealers pay us the interest. In the case of treasury bills, the interest is derived from the interest on government of Canada treasury bills.

Mr. LAMBERT: Will this form of secondary reserve continue under this act?

Mr. HACKETT: Yes.

Mr. LAMBERT: There is no change?

Mr. HACKETT: There is no change as to the constituents. There is change as to the ratio which we will be required to carry.

The CHAIRMAN: Mr. Lambert if you have terminated your questioning, I would like to recognize Mr. Lind.

Mr. LIND: I was wondering, Mr. Chairman, if I could just ask a couple of questions now and continue in my position after we reconvene as I have another engagement at a quarter to one.

The CHAIRMAN: Well, go ahead.



Mr. LIND: I am interested in this secondary reserve, Mr. Chairman. My question is to Mr. Hackett. I am rather in the dark with regard to these day to day loans to the money market. I just do not understand what you mean when you say the interest changes hour by hour. Where is this to, the bond market, the security market or the stock brokers? Where is this money loaned?

Mr. HACKETT: I am afraid it may take a few minutes to give Mr. Lind an adequate reply but subject to that, the day to day loans are made to money market dealers. I can never remember whether there are 15 or 16. I think it is 15. These are investment dealers. In no case is this their sole function. They all have other activities. They became money market dealers by agreement with the Bank of Canada. The actual nature of that agreement is something of which we are not aware but I think it is safe to say broadly that these are dealers who have demonstrated their willingness and ability to maintain active markets in short term government securities, including government of Canada treasury bills.

Once they become money market dealers, each dealer has a line of credit with the Bank of Canada. This facility being in existence, it is a way in which any one chartered bank may quickly adjust its cash. If I were in my own office this morning and I saw I had more cash than I appeared to need at the time I would offer, or more particularly one of our money traders would offer, to these money market dealers, day to day money. That is a loan secured by government of Canada bonds of three years maturity or less or by banker's acceptances, so long as they are not your own. This is a very impersonal market; it is a very fluid market. Therefore, to accomplish one's purpose one has to offer this money at a rate at which one thinks it will be attractive to the dealers who wish to borrow it. What that rate may be will depend on the size of the inventory of government of Canada bonds of three year's maturity or less which includes treasury bills which a particular dealer has to carry and wants to carry at the moment. The rate will also be influenced by the number of banks that happen to be offering money at that point of time. To get your money out you may have to offer down. It is a little bit like a Dutch auction.

If on the following day the position has changed in the clearing and you want your money back the bank concerned will then call day to day loans from the dealers. That call has to be made by 12 o'clock noon. The dealer whose loan is called—this is still a very impersonal operation—has to get on the telephone and find another bank who is a lender. Generally speaking the fact that one bank is short of cash, the chances are that some other bank in the system will be long on cash and therefore the loan you call is probably picked up by some other bank or banks. Meanwhile this matter of negotiation as to rate is continuously going on. The rate may change two or three times in an hour or two hours. It is a rather interesting operation in that respect.

If there happens to be a general shortage of bank cash at that time and the dealer cannot find another bank as a lender or another bank or banks as lenders in sufficient amount, then the dealer or dealers will look around the street for alternative sources of lending. They might even go to one of the near banks. If other sources prove unavailing, then they take advantage of their line of credit with the Bank of Canada and go in and obtain temporary accommodation from the Bank of Canada at a penalty rate.

Tonight, at five o'clock, when the Bank of Canada weekly balance sheet is released we shall be able to look at that balance sheet and see the extent, if any, to which money market dealers are, as we say, into the Bank of Canada. Now when the dealers are borrowing from the Bank of Canada indicates a situation when for some reason or another there is a state of temporary stringency in the banking system. It may be a very temporary thing, but the fact that the dealer has to go in means that he cannot get his loan requirements from the banking system at that moment of time. The next day it may be a quite different situation. It is a very fluid procedure but it is a great convenience to the banks in assisting them to keep the cash well distributed through the system. It does not work perfectly. There are many times when a banker or indeed, the banks as a whole, will wish to employ cash and the demand will not be there. It has its imperfections but by and large it serves a useful purpose.

Mr. LIND: Mr. Chairman, I was wondering if I could ask one short question and then be permitted to leave and resume after we reconvene. Am I on the first of the list for later?

The CHAIRMAN: If we are still on this topic when you return.

Mr. LIND: Well, I would like to remain on this topic. I would like to have the privilege of resuming this questioning after 3.45.

The CHAIRMAN: The other names on my list, unless I misunderstood their signals, are Mr. Laflamme and Mr. Addison, and Mr. Gilbert as well. Actually, Mr. Hackett has made this market operation so fascinating I am wondering if you would like to go down and watch it being carried out.

Mr. HACKETT: It would indeed be fascinating. We would be very glad to have you come.

Mr. LIND: I am just asking for that privilege, Mr. Chairman.

The CHAIRMAN: This will create no problem. I gather you have to leave right now and perhaps if we take Mr. Laflamme and since Mr. Gilbert has some questions it will merely involve your being available when we resume this afternoon.

Mr. LAFLAMME: I do not know, Mr. Chairman, to whom I should direct my questions but it is regarding clause 72 of the bill. I see there is a great difference there between the requirements of the Bank of Canada for the primary reserves and the secondary reserves. Clause (72(1) says that the bank "shall" maintain a cash reserve. When they speak of secondary reserves in subclause (2) they say the bank "if so required by the Bank of Canada". Is it not a fact that possibly the Bank of Canada should increase the secondary reserve, but is it not in itself a way of having better control over the money market by the Bank of Canada?

Mr. HACKETT: Well, Mr. Laflamme, it is certainly one way through which a very major degree of control could be exercised. The fact that the range of variation is so wide does, we suggest, introduce quite a new element of uncertainty into the cash management, investment management and indeed, loan management of the banks. If I might digress, for one moment, it is a pretty potent reason why we find this two weeks averaging period a little unrealistic. This is one way through which the Bank of Canada could transmit influence to

the central bank which would cause some kind of a shift in the asset mix. I beg your pardon, it is some way in which the Bank of Canada could transmit influences to the chartered banks which would cause the chartered banks to make some kind of a change in their asset mix.

Now, we are of the view that if this be an emergency standby device, then in the context of the kind of emergencies that could arise a better, smoother and more precise result could be obtained by discussion with the banks and their co-operation sought to the extent and in the particular directions necessary to meet the specific requirement of the situation at the time, rather than by bringing a statutory power to bear on one particular group of assets. If a bank individually, or the banking system, and in this context it would be the banking system, is under pressure, make no mistake about it, the banking system is going to have to make some kind of a change in its assets to respond to Bank of Canada policy.

But is that not a question whether from the standpoint of getting a smooth response and getting the kind of response you want, which may be quite different under different circumstances, this rather mechanical device, this shotgun approach, is perhaps the best way of going about it. I should, perhaps, add too—I think this bears on this matter—that one of the difficulties of this statutory secondary reserve ratio is that it sets up by legal fiat what secondary reserves are. Now, banks have other assets which are perhaps just as liquid as these legally defined liquid assets.

The CHAIRMAN: May I interrupt here. Does the law create now a definition of primary reserves which other students of the matter may feel should be broadened or narrowed to include other amounts than the law presently requires?

Mr. HACKETT: I think there is a range of discussion there, sir. For example, the law may say that the banks have to have a certain body of secondary reserves as defined in this act. You do run into anomalies.

The CHAIRMAN: My point is that the same problem could be raised if there is a problem with respect to primary reserves.

Mr. HACKETT: The primary reserve is cash, sir.

The CHAIRMAN: No, but my point is if you look at clause 72, there is a definition there. It is not a major point but I just want to make this comment if Mr. Laflamme would be kind enough to let me intervene. Let me put it this way. I am wondering whether it is justifiable to raise as a possible complaint that the secondary reserves are defined by law when this is already being done with respect to primary reserves?

Mr. HACKETT: I do not know that it was a complaint, Mr. Chairman, as much as an observation.

The CHAIRMAN: That is the better word I was seeking.

(Translation)

That is "le mot juste" as we say in French.

(English)

I think observation is a better word.



Mr. HACKETT: Perhaps I could clarify the point to show its relevance in this way. There is an issue of government of Canada bonds that matures on the 15th of December. Those bonds have about three weeks to run. They are not part of our liquidity. They may, in effect, be much more liquid than a treasury bill with six months to run which is defined as part of our liquidity. My only point in raising this was that after all, this is an arbitrarily defined area we are speaking of.

The CHAIRMAN: My point is, this covers the whole area of reserves in general, in so far as the requirements are imposed by law. You have to have a definition.

Mr. HACKETT: In so far as the act requires, yes. In so far as banking practice is concerned, not necessarily.

Mr. LAFLAMME: I have one final question on that. The chartered banks in this proposed legislation are empowered to sell debentures, and in clause 72(1) the cash reserve ratio is lowered. Is it not in the interests of better control of credit for the Bank of Canada under clause 3 to require the chartered banks if necessary to keep a certain average of secondary reserves. If you accept the fact that the Bank of Canada must control credit I do not see why you should—I will not say complain—not be in agreement with the Bank of Canada. Do you really think that the Bank of Canada would require secondary reserves which would not be in the interest of the Canadian public?

Mr. PATON: I think, Mr. Laflamme, we express our feeling fairly definitely in this brief in which we quote the Porter Commission as saying that they examined the contention that the Bank of Canada should have legislative power on secondary reserves and, “they are not persuaded that any legislative power to direct allocation of the institutions’ funds is necessary.” As you know, we are operating under a voluntary secondary reserve currently—

Mr. LAFLAMME: Yes.

Mr. PATON: —which as we referred to once before, was brought in at a time of financial crisis shall we say: and which has remained steady notwithstanding the disappearance of that crisis period. This new legislation further cements this provision of secondary reserve, admittedly referred to as being on a standby basis; but, it does make it in legislative form. The chartered banks support the Porter recommendations in this respect, that we do not consider it a necessary arm of the Bank of Canada’s control over our operations.

Mr. LAFLAMME: Yes, but there will still be a great difference between an obligation and a possibility.

Mr. PATON: We are legislating for ten years.

Mr. LAFLAMME: Yes. Thank you, Mr. Chairman.

The CHAIRMAN: I declare this meeting recessed until 3.45 this afternoon.

#### (AFTERNOON SITTING)

The CHAIRMAN: The meeting is now resumed.

We have something to straighten out here. Mr. Lind, as you may recall, was not able to complete his questioning because of an appointment he had, and

although Mr. Gilbert was the one to follow Mr. Laflamme, I wonder if he would be willing to yield for a few moments to Mr. Lind?

Mr. LIND: I think, Mr. Chairman, we were questioning Mr. Hackett with regard to the day-to-day loans. He gave quite an extensive description of how these money market dealers operate.

What I am very interested in, unless it is a trade secret, is the range of interest that these people pay on these day-to-day loans.

Mr. HACKETT: You mean the range of interest rates?

Mr. LIND: Yes; I do not mean any particular day, but just from the top to the bottom.

Mr. HACKETT: Well, since inception—and I speak subject to memory and correction—this range has varied in response to market conditions, and particularly in response to the market rate on government of Canada treasury bills, from, I would say, on the low end of the scale, perhaps a  $\frac{1}{2}$  but certainly  $\frac{3}{4}$  of 1 per cent up to as high as 6 per cent.

Mr. LIND: This is figured on a daily basis?

Mr. HACKETT: No, sir; the range on any one day would not be anything like that. I am speaking now of the spectrum of rates since the technique was introduced.

In one single day it is conceivable that the range might be—and it might move in steps of  $\frac{1}{8}$  of 1 per cent at a time—a total of  $\frac{1}{2}$  to possibly  $\frac{3}{4}$  of 1 percentage point, depending on the forces of supply and demand at work at the time.

Mr. LIND: What is roughly the range now? Would it be 3 per cent or 2 per cent or 4 per cent?

Mr. HACKETT: No; at the present time—and I have been away from the office, as you know—but probably between  $4\frac{3}{4}$  and  $5\frac{1}{8}$  per cent, or something of that order.

Mr. LIND: Thank you very much.

You say in your brief at page eight:

As the chartered banks are not paid any interest on their deposits with the central bank, now in excess of \$1 billion, any reserves required by statute in excess of the actual operating needs...

—and this is where I would like to ask you the question—

represents a continuing loss of earnings by the banks and a continuing element of discriminatory treatment relative to competing institutions not subject to legal reserve requirements

Now, could you explain what these discriminations are?

Mr. HACKETT: I would suggest, Mr. Lind, that the discrimination is twofold. In the first place, the competing near-banks institutions need only to carry as cash reserve what they deem their operating requirements to be. Secondly, the competing near-bank institutions do not maintain their cash reserves in the form of deposits with the Bank of Canada; by and large they maintain them with

deposits with the chartered banks on which they obtain interest. So that they carry less and they get interest on what they do carry.

Mr. LIND: Do you mean that a trust company, Mr. Hackett, probably keeps 3 per cent in coinage in its bank, and on the balance that it borrows from the bank through which it is operating it receives an interest payment from the bank for this reserve that they carry there?

Mr. HACKETT: They would not keep the cash in coinage, Mr. Lind, except to the extent that they require till money. The point is that, with regard to any other cash reserves that they may wish to keep, the near-bank is at liberty to make any kind of arrangement it wishes for the keeping and deposit of its cash reserves.

Mr. LIND: Is it not a recognized fact that they do keep in short term bonds in the neighbourhood of 20 per cent. They keep a higher percentage than the banks do although they may not keep as much coinage or cash reserve as the banks do, but they do keep reserve in short term bonds, for liquidity.

Mr. HACKETT: As I recall, Mr. Lind, there was placed before us, earlier on in the sessions, a consolidated statement of the trust companies. I do not have it at hand here—

Mr. LIND: I have that consolidated statement, but I was asking you for an opinion.

Mr. HACKETT: I would hate to generalize on this, but I would doubt if, by and large, the near-banks would carry more assets that would be comparable to the chartered banks' mix of cash, secondary reserves and government securities than would the chartered banks. I would hesitate to say that they did in the absence of a balance sheet which would give us that figure.

Mr. LIND: You doubt that they would carry more than the chartered banks.

Mr. HACKETT: Yes; I would doubt that, Mr. Lind.

Mr. LIND: Well, on discussing some of the problems with them, they tell me that they carry within the area of 20 per cent. Now, it is not all cash reserves, as we have been talking about, but it would be in short term bonds and something that they could consider as immediate liquid assets.

Mr. HACKETT: Well, accepting that figure, sir, I think we can make some sort of a comparison. Now I can speak with a fair degree of accuracy. Taking the chartered banking system as a whole—and we do have weekly figures on this, and there will be a fresh set of them published by the Bank of Canada late this afternoon—on that basis I would say that the cash liquidity and government of Canada securities of the chartered banks would be of the order of 29 per cent of their deposit liabilities—somewhere in that order; it might be 30 per cent or it might be 28 per cent but it would not be outside that range; which would be somewhat more than the figure you suggest for the trust companies.

Mr. LIND: Then the chartered banks, if they wish, could sell 10 per cent of that and still be 2 per cent over the requirements, and extend credit to small businesses and so on could they not?

Mr. HACKETT: The statutory requirements, sir, apply to cash, day-to-day loans and treasury bills.



Mr. LIND: But you are only forced by law to keep 15 per cent, are you not?

Mr. HACKETT: At the present time we are not forced by law. We do so by agreement with the Bank of Canada.

Mr. LIND: It was my understanding that you had to keep 8 per cent in cash reserves.

Mr. HACKETT: The secondary reserve portion is by agreement with the Bank of Canada, not by law at the present time.

Mr. LIND: Having the 7 per cent there?

Mr. HACKETT: Yes.

Mr. LIND: Then why do you use the word "discriminatory" at all, because you have the option of reducing that if you want to?

Mr. HACKETT: With respect to the liquidity portion of this, that is, cash, day-to-day loans and treasury bills, as far as the statutory portion is concerned—the cash reserve—we do not have any option. As far as the secondary reserve portion is concerned, we have given an undertaking to the Bank of Canada to maintain that ratio, and the only option we would have there is if we chose to break our undertaking, which we have never done.

Mr. LIND: Let me get this clear. You give an undertaking to keep 29 per cent, roughly; is that it?

Mr. HACKETT: No, sir; I am now speaking of liquidity reserves. There is no undertaking with respect to the amount of government securities that we maintain except in so far as it applies to treasury bills, which are part of our liquidity.

Mr. LIND: Carrying on down page 9, there is the statement:

... the Association remains of the view that statutory provision for secondary reserve requirements is neither necessary nor desirable.

I think that refers to your excess of cash, government of Canada treasury bills and day-to-day loans to the market?

Mr. HACKETT: That is right.

Mr. LIND: Now, why is that not desirable?

Mr. HACKETT: This will entail a repetition of some of the points made this morning, and I will bear that in mind as I go along.

As I endeavoured to make clear this morning, each bank would undoubtedly carry some secondary reserves. But here is a case where the assets that we are entitled to call secondary reserves are defined by law regardless of the fact that we may have other short term assets, such as short term government bonds, which are just as liquid but which are not in this category. To the extent that the deployment, or mix, of the assets of a bank, or the banking system, is held to what we regard as an unnecessarily high degree in these relatively low-yielding assets, there is an element of discrimination vis-à-vis other financial institutions which are not required by law to maintain short term assets in this particular way.

There is another and rather more subtle element of potential discrimination in this, particularly under the new technique that is envisaged in the present bill.

At the present time 1 per cent of the chartered banks' Canadian deposit liabilities is, in round figures, \$190 million. Let us assume, for the sake of argument, that this requirement within the ambit of the act is raised by 1 percentage point. This would presumably mean that the banking system would have to go out and acquire an extra \$190 million of day-to-day loans or treasury bills. But an interesting question arises: What would happen if the market could not supply those? As of last week, for example, the floating supply of treasury bills outside of the Bank of Canada, the chartered banks and government accounts, was only \$148 million, and that included the amount that was held by dealers. Now, to the extent that the market would not supply you with this additional, required liquidity, the banks would then have to fulfill their requirements by holding cash, which would increase the non-earning portion of the liquidity to an unnecessary degree.

Mr. LIND: One further question, Mr. Chairman. Is this normal though—

The CHAIRMAN: Mr. Lind, would you yield to a supplementary question from Mr. Fulton?

Mr. FULTON: I have, since Mr. Lind is questioning on the amounts. The banks are presently holding 15 per cent over-all reserves with the Bank of Canada?

Mr. HACKETT: Cash and secondary reserves. Actually we are presently maintaining somewhat more than that, because since you have to maintain 15 per cent, to get free or usable liquidity you would have to go a bit beyond that.

Mr. FULTON: Yes. Am I right in my interpretation that the effect of clause 72(3) under the new proposed bill with new clause 18(2) of the Bank of Canada bill, may be to require you to maintain as much as 18 per cent? That is taking account of the 12 per cent on demand deposits plus the 6 per cent secondary reserve which seems to be contemplated under clause 18(2) of the Bank of Canada bill.

Mr. HACKETT: A little bit more than that, Mr. Fulton, if you want to be accurate about it. I think it has been stated here that the average cash requirement would be about 6.60 so we could call it 18.60 or 18 $\frac{3}{4}$ , or something like that.

Mr. FULTON: So that the required reserves in this category of demand deposits with the Bank of Canada will be more under the new proposal than it is at present under the statutory plus voluntary arrangement.

Mr. HACKETT: On the demand deposits, Mr. Fulton, it could be considerably more, because the cash reserve ratio against demand would be 12 per cent. Against demand deposits it is 12 per cent and against notice deposits it is 4 per cent. I am sorry; I understood your question to relate directly to demand deposits.

Mr. FULTON: I say that under the new proposal, when read in the light of clause 18(2) of the Bank of Canada bill, the minimum secondary reserve is 6 per cent, so that makes a—

Mr. HACKETT: Well, there is a range there which the Bank of Canada may apply at its discretion, and that range runs from 6 per cent to 12 per cent. I am putting it at the outside.

Mr. FULTON: The minimum, then, is 6 per cent, is it not?

Mr. HACKETT: That is right; the maximum is 12 per cent.

Mr. FULTON: So that the minimum reserve you will be required to keep on demand deposits is 18 per cent and the maximum may be 24 per cent?

Mr. HACKETT: I would like to correct that. According to the bill, conceivably the Bank of Canada might require a zero secondary reserve requirement, but subclause (a) then states that when no percentage is in effect for any month the Bank shall not fix a percentage greater than 6 per cent for the next following month.

Mr. J. H. COLEMAN (*Vice President, The Canadian Bankers' Association*): In other words they cannot go from zero to 10 or 12. They can only go to 6 per cent in one month.

The CHAIRMAN: Mr. Lind, I do not want to—

Mr. FULTON: May I just finish? Whenever a secondary reserve is called for the minimum with respect to demand deposits will be 18 per cent?

Mr. HACKETT: No, sir. The maximum potential reserve under the act with respect to demand deposits is a statutory 12 per cent cash—and that does not vary; that is there—plus, conceivably, under the act, a 12 per cent secondary. So that would be a total of 24 per cent.

Mr. FULTON: So this is the maximum figure.

The CHAIRMAN: Mr. Lind, even taking into account Mr. Fulton's supplementary questions and adding in your time at our morning session, I think you have had about 20 minutes.

Mr. LIND: I cannot see how. I will argue that point with you, because I only had five minutes before, and we did not start until about seven minutes after.

The CHAIRMAN: The clerk has 3.55 marked down as the time you began your very interesting questions. Do you have a further question?

Mr. LIND: No, I am through.

The CHAIRMAN: Mr. Gilbert?

Mr. CLERMONT: Would Mr. Gilbert permit me to ask a supplementary question? Mr. Hackett said that the reserve may go as high as 24 per cent?

Mr. HACKETT: Under the bill, Mr. Clermont, the fixed reserve against demand deposits in cash is 12 per cent; on top of that the Bank of Canada has power to impose a 12 per cent secondary reserve; if we are considering the combined reserves it is 24 per cent.

Mr. CLERMONT: Yes; but what about the 4 per cent and the 12 per cent? I mean, there are two kinds of reserves, 4 per cent in one case and 12 per cent, which will give a minimum of 6.6 or 6.7.

Mr. HACKETT: Yes, Mr. Clermont. I was answering Mr. Fulton's question in the context of his inquiry about what was the ratio against demand deposits alone. On average deposits, you are quite right.

The CHAIRMAN: Mr. Gilbert?



Mr. GILBERT: Mr. Chairman, I am going to ask Mr. Hackett a very short question. How serious are the Canadian Bankers' Association in their contention with regard to the fortnightly average in the new provision, as compared to the monthly averaging with regard to the formula of determining cash ratios? I am going to point out to you the contention of the Bank of Canada, set forth in their brief to the royal commission, and I am going to read the conclusion first. It says:

The present view of the Bank of Canada is that the existing formula permits unduly slow responses and results in unduly large discontinuities in cash reserve requirements.

And, to direct the reasoning for that to Mr. Lambert, who asked you why the central bank was so concerned about it, they mention at page 142:

It is highly desirable that there should be some short-run elasticity in the "money supply" so that the banking system can quickly absorb the day-to-day shocks that result from sudden changes in the demand for credit or in the attitudes and desire for liquidity of investors or from sudden shifts in cash between banks. It is impossible for the central bank to know about all the factors that produce such developments in time for it to make the necessary adjustments in cash reserves...

Now, here you have a view expressed by the central bank with regard to slow responses as a result of the monthly averaging, and a direction by them that in order to maintain control over the monetary policy they feel it is better to have it on a fortnightly basis. Just how serious can you be with regard to wanting to co-operate with the central bank in determining monetary policy?

Mr. HACKETT: I think, possibly, there are two questions there. To answer the first one, I would say that we were very serious indeed. Again, at the risk of repetition, I would emphasize that there is no difference of view between the chartered banks and the central bank on the objective which the central bank is seeking to achieve.

I might, perhaps, add by way of comment, that if the central bank has difficulty in ascertaining which way cash is going to jump—and they see the whole picture—one individual bank is certainly going to have difficulty in assessing the impact of the myriad cash load that affects its position from one day to the next. We do not see as much of the picture as they do. Therefore, each bank is endeavouring to work as close to its cash limit as it can, and I should emphasize, Mr. Lambert, that it is in the dollar and cents interest of the banks so to do. There is no percentage in sitting on cash just for the sake of sitting on it. When we find ourselves running a cash reserve on one day, or perhaps two days in a row, that is high enough, perhaps, to elicit the curiosity of the central bank about why we are doing it, and there can only be one of two reasons. The first is that we are anticipating something that the Bank of Canada may not know about, and the other is we are trying to employ it and cannot. That situation does arise from time to time.

Mr. GILBERT: In substance, I think we can appreciate the problem of the Bank of Canada in trying to determine the response to these changes, or, as they say, the sudden shocks which are almost daily. Here is the over-all picture. This is their basic reason for wanting this provision to change it to fortnightly averaging.

Mr. HACKETT: I doubt the Bank of Canada would maintain that these sudden shocks are almost daily. I think that in most cases these deviations from the norm for any bank in respect of a cash ratio are relatively rare, and they arise out of these unforeseen and unforeseeable situations which face us every now and then.

I think the distinction you make, really, is a distinction that might be made on the part of any people who have to live and work in this medium. We appreciate the Bank of Canada's problem. Perhaps we should appreciate it more if we were sitting where they sit. Perhaps they would appreciate ours more if they sat where we sit. But it is the case that we have to deal with uncertainty. If we did not, every bank would run a continuous 8 per cent. Secondly, the market is just not sufficiently responsive to enable every bank to do all that it wants to do when it wants to do it and in the amount that it wishes to do it.

Mr. GILBERT: Thank you, Mr. Hackett.

The CHAIRMAN: The next name I have on my list is that of Mr. Lambert.

Mr. LAMBERT: My only comment in relation to the last exchange is that, having read what the Bank of Canada said, I am wondering, perhaps, when they come here, if we will find out that their fears are more theoretical than actual in this regard.

Mr. GILBERT: I thought I had better point out to him what they had to say, because you had asked that question, why the central bank—

Mr. LAMBERT: Oh, but I meant in actual bumps, not theoretical ones—actual difficulties in this regard that the Bank of Canada had experienced in its past few years in actual monetary control, through which they had felt themselves to be hampered and as a result of which the monetary system had suffered, and not merely to introduce change for the sake of change on some theoretical grounds.

Mr. GILBERT: We will await Mr. Rasminký's return.

Mr. LAMBERT: Yes, very definitely.

Mr. HACKETT: Perhaps I did not quite clarify it, Mr. Chairman. I would like, in respect of those two comments, to add that we fear that these bumps will not be eliminated; that they will, if anything, be aggravated.

Mr. LAMBERT: To make absolutely clear what you were saying to Mr. Fulton, it is right, though, that, under the new requirements, against the demand deposits there can be reserve requirements up to 24 per cent ranging from the 12 per cent in cash primary reserves and anything from .01 all the way up to 12 per cent over the period of time allowed under clause 18(2)(c) of the Bank of Canada bill?

Mr. HACKETT: Yes, at the top end of the range.

Mr. LAMBERT: I think that is all I have to say on this.

The CHAIRMAN: Mr. Johnston?

Mr. JOHNSTON: I have one question for the clarification of the wording in clause 72(1)(b). Does the expression "deposit liabilities" there include debentures issued by a chartered bank or near-bank, mortgages issued by a mortgage loan company or a chartered bank, or other long term investments?

Mr. HACKETT: With respect to the mortgages and the investments, those would be assets, and this reserve ratio applies to liabilities; so that they do not enter into it. With respect to liabilities in the form of subordinated debentures, the cash reserve requirements do not apply.

The CHAIRMAN: Have you completed your questions, Mr. Johnston?

Mr. JOHNSTON: Yes.

The CHAIRMAN: I have no further names on my list. I therefore propose that we move on to the next topic, headed "Limitations on Bank Participation in Other Corporate Ventures". Are there any further questions on this topic at this time?

Mr. Lambert?

Mr. LAMBERT: There is an exception in the bill—and it is a curious one, I must say—that although it lays down that the bank shall not have any more than a 10 per-cent corporate holding in any corporation as a long term holding for purposes of its business, yet it can acquire shares in a corporation in satisfaction of, say, a bad debt, or as an item of collection, and it can hold on to these shares *ad infinitum*.

Mr. ELDERKIN: May I interject, Mr. Lambert, at this stage? This matter was raised previously. It has been discussed, and in all probability we will be bringing forth an amendment on this.

Mr. LAMBERT: Oh, I see; the rules of the game are being changed.

Mr. ELDERKIN: We change them all the time.

The CHAIRMAN: In other words, the discussions of the Committee have already been useful, in fact.

Mr. LAMBERT: To what extent? Are the banks going to be forced into a fire sale of these securities that they acquire, say, in the liquidation of a bad debt account?

Mr. ELDERKIN: I would think, probably, it would follow the same provisions, Mr. Lambert that affect real estate acquired in the liquidation of a loan, namely that they will be given a period of years to dispose of it. This applies now, as you realize, to any real estate required in the liquidation of a loan. Under the act they are given 12 years to dispose of it, otherwise it is subject to forfeiture to the Crown.

Mr. LAMBERT: Will the provisions be any more stringent for the chartered banks than they are for the trust companies under the Trust Companies Act?

The CHAIRMAN: I would suggest that perhaps we ought to wait until we see the terms of the amendment. We may be getting into the area of policy.

Mr. LAMBERT: No, this is a factual comparison. I am asking are they going to be any different. After all, in the Trust Companies Act there is a period of years.

Mr. ELDERKIN: Twelve years.

Mr. LAMBERT: Twelve years; and this will be a parallel provision.

Mr. ELDERKIN: Close to a parallel provision.



Mr. FULTON: While you are on this question of the amendment I would like to make an observation. I would have preferred, and hoped, to see the amendment going the other way, rather than tightening up the provision by tightening up the loophole, to undo the proposal that makes it necessary to look for loopholes. You are sure you would not consider the amendment going in the other direction.

Mr. ELDERKIN: It is not what I consider, Mr. Fulton.

The CHAIRMAN: Perhaps Mr. Elderkin can note your suggestion.

Mr. LAMBERT: I put some questions the other day with regard to the maintenance of a broad base of operations for a bank's activities, and suggested that if the bank could thereby move into profitable areas of operation it would be under less pressure to concentrate on the narrow gap in, shall we say, its commercial banking operations where the extent of its success is the maintenance of as wide a gap between the cost to it of funds and the net revenues it obtains from its customers. Now, it is my view that this is a retrograde step that is proposed in the bill, merely because it concentrates the banks' activities more and more into a narrower compass and makes it that much more difficult for the banks to develop. Have you any observations to make?

Mr. PATON: Mr. Lambert, our feeling is that this is a further restriction, not particularly for the purpose to which you refer, but because what we have done in this area to date has been beneficial to the economy of the country. Conceivably, there could be opportunities, not yet envisaged, over the next decade for us to expand our interest into areas outside our specific banking operation. Therefore, we would strongly urge that these limitations not be continued in the bill and that permission should be given to the banks to take such steps as they currently see necessary, within the ambit of the bill as we now have it, to avoid being limited in performing functions which we think we could justify as the economic situation changes. I think we point that out even in the exception regarding bank participation in the export finance corporation which is a government-encouraged corporation, that there may be other areas of that nature where we could usefully facilitate the trade of this country. Certainly this would be our primary desire.

Our secondary desire would be that, if there is a limitation on future participations, any participation taken to date should be left untouched.

Thirdly, if that is not possible, any of the retroactive measures that might have to be implemented should not be as general as indicated in Bill No. C-222.

Mr. Coleman, have you anything to add to that?

Mr. COLEMAN: No, I think that covers it.

The CHAIRMAN: Mr. Fulton?

Mr. FULTON: Perhaps Mr. Elderkin might want to answer the first question.

Here we have a provision which is going to force the banks to sell their holdings in these other corporations down to 10 per cent. I would like to know where that leaves them with respect to their competitors, the trust companies. Can you tell me—because I do not know—if trust companies are allowed to hold more than 10 per cent in other corporations?

The CHAIRMAN: Mr. Elderkin, are you in a position to answer that?

Mr. ELDERKIN: They, of course, have a very much more restricted investment portfolio than the banks except within their basket clause by which they can hold anything they want to.

Mr. FULTON: Yes; but I do not think, for instance, that the Royal Bank and the Banque Canadienne Nationale regard their holdings of shares in RoyNat as part of their ordinary investments, do they?

Mr. ELDERKIN: They are treated as such on their balance sheet.

Mr. FULTON: There are trust companies in RoyNat, are there not?

Mr. ELDERKIN: Yes.

Mr. FULTON: So that they can go into that. Is there any limitation requiring them not to hold more than 10 per cent?

Mr. ELDERKIN: I cannot answer that, Mr. Fulton. I can find out for you later.

The CHAIRMAN: At the same time the federally incorporated trust companies are limited in the total amount of common shares they can hold. We have had this percentage before. Perhaps you could refresh my memory if nobody else's. Do you recall what that is?

Mr. ELDERKIN: No, I do not, but I will find out and report back to the committee on this.

Mr. FULTON: Yesterday we heard from Mr. Paton the view that, to put it mildly, it was with extreme reluctance that the bankers' association would wish to give a list of their holdings in companies that would be affected under this clause. As I understand it, one of your main concerns is that if the provision stands and becomes law there may be considerable enforced activity in marketing the shares of the companies and you felt that it would possibly prejudice that operation to disclose what the extent would be. I think that is a valid point. Although I think it puts us under some inhibitions here with respect to discussion, for myself, at this time anyhow, I am not going to press for a named list.

However, I am wondering if, perhaps, you can answer some general questions. We have heard reference to two companies, RoyNat and Kinross. Do you feel free to say whether there are several, or just one or two other, similar relationships that would be affected? I am not thinking of holdings in trust companies; I am thinking of holdings in commercial operations.

Mr. PATON: Without having a specific knowledge of the other banks' involvements, Mr. Fulton, I think that "several" would be a reasonable adjective to use. In my own institution, for example, I know of two that would be in a similar area to RoyNat and Kinross, so I would think that there would be several among all the banks.

Mr. FULTON: Speaking for myself, and without any expertise, I would like to express an opinion and ask for your comment on it. I can see, in the light of the Porter Commission recommendations and in the light of the move being made towards increasing the competitive position of the banks, that there is a case to be made for banks to divest themselves of holdings in trust companies. I am unable to see any similar case for the banks having to divest themselves of holdings in companies like RoyNat. My approach to the legislation at the moment

is along those lines. Would you care to comment on whether, from your point of view, that is a reasonable differentiation to make?

Mr. PATON: I think that was probably the third point I made earlier, Mr. Fulton, that if there had to be restrictions we would like them limited to the class of business that perhaps has been concerning the government in their policy in introducing Bill No. C-222.

The other alternative is to permit the continuation of the holding of these shares to be under governmental discretion—and by that, I am referring to existing situations. There is a limitation of two years, as you will see in this brief. Perhaps, as a final concession, this two year area might be eliminated so that governmental discretion could be used in taking a decision on whether continuation of the holding of X company by Y bank would or would not be inimical in the best interest of the country's economy.

Mr. FULTON: With respect to the operations themselves, it has been pointed out to us that under the new legislation the banks can go into the mortgage lending field directly, and that they can issue debentures to get their long term source of funds for this type of financing. I take it that in theory the banks could carry on, as banks, a type of operation that is now being carried on by one or more of these companies, or corporations. I think Mr. Coleman started to develop—but I got the impression he did not complete it—why, in your view, it is more advantageous—I take it this is your view—that it should be done, as it were, by a subsidiary or controlled corporation rather than by the bank as a bank. What grounds of convenience, administrative and so on, do you...?

Mr. COLEMAN: Mr. Fulton, our bank proposes to submit a brief. Mr. McLaughlin will be here to discuss RoyNat.

I could go into this now, but perhaps the Chairman would feel it would be taking up the time of the committee, since this particular subject and its ramifications will be discussed at some length when Mr. McLaughlin speaks to the brief.

The CHAIRMAN: Yes, anticipating the brief—

Mr. FULTON: I have read it, and I did not want to anticipate that, but Mr. McLaughlin, I assume, although he has had a broad general experience, will be specifically discussing RoyNat.

Mr. COLEMAN: That is right.

Mr. FULTON: This is his special concern, and I thought perhaps the association might care to express a general view.

Mr. COLEMAN: I think you will be discussing the principle. We, of course, have a selfish interest in RoyNat, but I would think Mr. McLaughlin will speak to the principle of the legislation rather than specifically. He will talk specifically of RoyNat, but he will be interested in the principle.

Mr. FULTON: I am quite willing to defer that question, Mr. Chairman, if you think it might be better.

Mr. COLEMAN: I would be very happy, if you feel, Mr. Chairman, that I could enlarge on it.

The CHAIRMAN: Well, due to the fact that we obviously will be having a discussion on not merely RoyNat as such but on the concept when Mr.



McLaughlin comes, perhaps the Committee will feel we should focus our attention on that topic when Mr. McLaughlin is with us.

I presume that the association as such has nothing to add, in a sense, to the policy views expressed in this brief with respect to firms such as RoyNat and Kinross?

Mr. PATON: That is correct.

Mr. FULTON: Then, I think, Mr. Chairman, if I have your permission, I would like to ask a related question which is not on this point precisely but I do not think it is covered specifically in the bankers' association submission and that is with respect to interlocking directorates. This is not dealing with controlled corporations.

The CHAIRMAN: You may as well ask the question. If it seems to be straying too far afield I will have to exercise my discretion.

Mr. FULTON: We did question Mr. Elderkin on the policy point of view behind this provision that would prevent the same person from serving as a director of both a trust company and a bank. As I recall it, Mr. Elderkin, with some reservation, expressed the opinion that this would be likely to have the result that trust companies would lose the services of these men rather than banks. Have you any confirming or dissenting opinion?

Mr. PATON: There probably would be a very difficult choice to be made individually by directors, Mr. Fulton.

I think we should, perhaps, reflect that these individuals serving on boards of both companies are very capable, competent business people drawn from industry right across the country and right across the whole gamut of industry. As such, they bring to each of the boards they are on a great amount of experience that is beneficial to the corporation they are serving.

I would be quite definite in my statement that the fact they are a director of both a bank and a near-bank in no way interferes with the operation of each company vis-à-vis the other. Speaking from my own personal experience the management of both the trust companies and the banks operate entirely independently of each other and, indeed, probably compete more aggressively, certainly in the last year or two, than perhaps they did in the past.

The CHAIRMAN: Mr. Paton, is it not difficult, almost by definition, to have a full degree of competition if the same individual is in the top management group, or at least on the board of directors?

Mr. PATON: I think, perhaps, one should have a pretty clear definition of management vis-à-vis the board of directors.

The CHAIRMAN: I am using the term "management" in the broad sense.

Mr. PATON: Management of the banks—

The CHAIRMAN: I am not talking about executive management. Is not the continuance of the present situation apt to put the directors who are on both types of boards in a more and more difficult situation if competition becomes more intense? You may go to a board meeting of a bank one day and of a trust company the next day. Decisions have to be taken which, although not confidential, might, if the knowledge was fully divulged to the opposing party, create a

reaction that would hamper the competition. How do you avoid that if the same people are on the two types of boards?

Mr. PATON: I would say this, that it certainly has not, in my opinion, had any detrimental effect so far, Mr. Chairman. I just cannot envisage it doing so. My reference to management is that in management in these separate corporations there is a very large degree of autonomy.

The CHAIRMAN: Do you mean to say these institutions are run without real reference to the board of directors?

An hon. MEMBER: That is what he means.

Mr. PATON: I do not think I quite mean that. I just want to get the balance properly weighted in the actual operation of both these types of institutions.

The CHAIRMAN: With all due respect to you, sir, the result must be one way or the other. Either management operates without reference to the boards or the boards have something to say about management, and if the same people are on the boards, people can legitimately ask questions about how the people on the boards will serve their respective interests.

Mr. FULTON: Would there not be at least a degree of protection, if not prevention, by the fact that certainly on any vote a director would have to declare any interest which might be adverse, and presumably in any event the rest of the board would know, with respect to director X, if he was a director of a trust company.

I will ask it as a question: Would that not be a factor that would inhibit him from pursuing matters designed to serve his interest in the other company?

The CHAIRMAN: Mr. Fulton, perhaps you can enlighten us on this. What about exchange of information? Take the case of the same person having access, as a director, to two sets of information which may be very useful from a competitive point of view?

Mr. FULTON: There, again, I should think that it is a matter of ethics. It would soon be known if, as a director of a bank, say, he gave them information that he derived in his capacity as a director of a trust company and it operated to the detriment of the trust company. This would not be secret for very long. I do not think he would stay as a director of the trust company, or, if it was in the reverse that he would stay as a director of the bank for very long. It seems to me that ordinary business precepts, which are not unethical, would prevent that.

The CHAIRMAN: Mr. Fulton, would that entitle me to be a member of the Conservative caucus while I am still a member of the Liberal party?

Mr. FULTON: I am of course not making any comparison between the ethics of the two institutions!

The CHAIRMAN: Let us hope that the bodies known as the caucuses have a reasonably high degree of ethical behaviour attached to them.

Mr. FULTON: In the sake of amity let us agree that the two are comparable.

Mr. Paton, are you in a position to tell us whether, in other jurisdictions, there are restrictions similar to those now proposed in Bill No. C-222?

Mr. PATON: I am not able to answer that question specifically.

Mr. COLEMAN: I do not think I understand your question.

Mr. FULTON: In the United States, the United Kingdom, or Germany are there similar prohibitions against the service of directors on more than one board?

Mr. COLEMAN: I am not able to answer that question. If there are, I have not heard of them.

The CHAIRMAN: We will ask one of our research officers to make a report on that.

Perhaps, Mr. Fulton, you could restate the question.

Mr. FULTON: I am wondering whether the United States, the United Kingdom, Germany and Italy—in areas or countries where the banking system is comparable, there is a prohibition on the service of directors similar to what is contemplated in Bill No. C-222.

Mr. COLEMAN: I could not answer the question, Mr. Fulton, no.

The CHAIRMAN: We have asked our research staff to take a note of that and report back. Do you have further questions?

Mr. FULTON: No, thank you.

Mr. ELDERKIN: May I interject then? I have just been handed the Trust Companies Act and subsection 11 of section 68 says:

Notwithstanding anything in this section, the amount of the company's investment or loans under the authority of this section in or upon the security of the debentures, bonds, stock and other securities of a company incorporated as aforesaid shall not exceed in the aggregate twenty per cent of the market value of the debentures, bonds, stock and other securities issued by such company.

That includes loans as well as securities.

*(Translation)*

Mr. CLERMONT: Mr. Chairman, in the recommendations by the Porter Commission, I think there is an important one to the effect that there should be more competition between banks and other financial institutions. Do you think, Mr. Lavoie, that the fact that the banks are not at present limited by a percentage of shares in other institutions, means, so to speak, that they can buy up their competitors?

Mr. LAVOIE: I don't understand your question too well, Mr. Clermont.

Mr. CLERMONT: Well, look, we are speaking about bank shares in other financial institutions?

Mr. LAVOIE: Yes.

Mr. CLERMONT: And the Porter Commission has it that there should be more competition between the banks and the financial institutions; the Commission thinks there is not enough at the present time. Don't you think that if there is a limitation of bank participation we won't have this competition?



Mr. LAVOIE: In my opinion if the banks are going to be allowed to continue to hold interests in other companies, this will certainly lead to greater competition. Roy-Nat, that was founded a few years ago has been I think of enormous assistance to the industry, particularly in so far as medium term loans are concerned. Let us suppose the banks got out of that sort of thing, I think that others would have to buy the interests in question, because I am convinced that such institutions are necessary.

Mr. CLERMONT: But again, Mr. Lavoie, when you claim that there is a good deal of competition among the banks, I think that I would not be going too far in saying that you are alone in claiming this. The Porter Commission thinks there is not enough and there are many other organizations who share that view. If you still have the right to participate in the management or to hold shares in other institutions, I don't see how you are going to get more competition that way.

Mr. LAVOIE: This matter of competition among banks is realistic, Mr. Clermont.

Mr. CLERMONT: It is realistic in view of the number of branches of banks in Canada?

Mr. LAVOIE: There are eight chartered banks in this country and I think that everyone of those tries to get the biggest share of business.

Mr. CLERMONT: You pay the same interest rate on deposits, don't you?

Mr. LAVOIE: Yes, Mr. Clermont.

Mr. CLERMONT: You call that competition when you pay the same rate of interest on deposits?

Mr. LAVOIE: We pay the same rate on savings deposits.

Mr. CLERMONT: Yes.

Mr. LAVOIE: And our branch managers are continually looking out for new business. This new business, most of it, comes to us from other banks.

Mr. CLERMONT: Yes, that could happen, because a loan can be refused and people feel they can make a better deal somewhere else.

Mr. LAVOIE: There is also a question of service. Every branch bank is organized to provide the best possible service.

Mr. CLERMONT: I don't think I would argue on this. I don't doubt at all about the service the banks give to the public, I am taking the experience of the Porter Commission which maintains that there is not enough competition at the present time in the banking system.

Mr. LAVOIE: In the present banking system, there is a lot of competition.

Mr. CLERMONT: The same thing has been repeated several times before this Committee when we started considering the request for new bank charters. The witnesses who came before us maintained that there was not enough competition.

Mr. LAVOIE: I don't feel that the present chartered banks are opposed to the establishment of new banks.

Mr. CLERMONT: No, because you were not here as a witness—but, the Bankers' Association would like the banks to continue to be entitled to have

interest in other institutions which might otherwise become competitors in the savings and deposits market?

Mr. LAVOIE: In our brief, we recommend that the chartered banks should stay in that field, particularly as far as companies already in existence are concerned.

Mr. CLERMONT: Don't you cover practically the whole field at the present time? The whole field that is open? Is there any possibility of adding very much to the present field of activity?

Mr. LAVOIE: I have brought the report of the Royal Commission on Banking and Finance, page 420, it is said that the banking industry is in many respects highly competitive in its continuous effort to improve service to customers. This seems to be something of an answer to a question you ask just now about competition.

Mr. CLERMONT: Well, I won't be long, Mr. Chairman, but you have quoted this paragraph and this is one of the reasons for changing the present Bank Act in order to increase the degree of competition in the banking system.

Mr. LAVOIE: I think that after the passage of this Act, Mr. Clermont, there will be no more question about agreements respecting interest on deposits and interest we charge to borrowers, I am sure that this is going to increase the competition between existing banks and even the new banks that are to come, those that are going to get charters shortly.

The CHAIRMAN: Have you finished your questions, Mr. Clermont?

(English)

I have no further names on my list.

Yes, Mr. Gilbert?

Mr. GILBERT: Mr. Chairman, I would like to have the solicitor for the Canadian Bankers' Association come forward. I would like to ask him some questions with regard to his understanding of particular clauses governing these corporate ventures.

Mr. LIND: Mr. Chairman, while he is doing that may I ask one question on competition?

The CHAIRMAN: Let us just get this sorted out. You are referring to clauses of the proposed bill dealing with this topic?

Mr. GILBERT: You are quite right.

Mr. CHAIRMAN: I believe that counsel for the association is here, a very distinguished member of the Canadian Bar, Mr. Cate. He has been in the audience, and perhaps too modestly keeping himself there. We should invite him to join his clients to deal with the technical-legal questions which I suspect Mr. Gilbert has in mind.

While Mr. Cate is coming to the witness' chair I would ask you, Mr. Lind, to pose your question.

Mr. LIND: My question is a very short one. Does your association control the hours for which banks are open for business in any province?

Mr. PATON: No, sir.

Mr. LIND: Why are they always the same?

Mr. PATON: They are not, actually, Mr. Lind. There is a certain uniformity, but at the present time they are not. They are not controlled by the association in any way, shape or form.

Mr. LIND: Is it not a fact that in any town they will adhere to the same hours.

Mr. PATON: That is correct.

Mr. LIND: There is a similarity in towns; and in areas—

Mr. PATON: There are different areas, yes. This is generally directed towards giving the best service to the customers.

Mr. LIND: Have there been any recommendations by the association to extend the hours so that people may have more convenient access in their use of banks?

Mr. PATON: There has been a trend in recent years, and certainly in recent months, towards the variation of hours in different localities and I would say that there is an indication there will be an impetus to this.

The CHAIRMAN: You mentioned that the reason for the existing hours is to give the best service to customers. Could you explain to me why a certain provincially-chartered savings and loan corporation in Windsor, which is open Saturdays, has long lines of people every Saturday coming in to make deposits and cash cheques? The place is thronged with people going in and out doing banking business of that sort.

Mr. PATON: I should perhaps—

An hon. MEMBER: Have you ever worked in a bank? Have you ever considered the staff?

The CHAIRMAN: They could still have maximum hours and the staff could take turns, working in various periods.

Mr. PATON: We maximize our efficiency and minimize our overhead so that our service to the Canadian public will be kept at the lowest level of cost, Mr. Chairman.

I would suggest, from experience, that the presence of large crowds in a banking office, or in a near-banking office does not necessarily mean good, profitable business for the institution.

Mr. LIND: I have one further question in this regard. On long holiday week ends, such as when Christmas and Boxing Day come together, what is the general policy of the banks in providing service to their customers when they can be closed for four days during the period?

Mr. PATON: Perhaps the coming Christmas festive season would be a good example of this, Mr. Lind, assuming we are through with this phase of the operation.

The CHAIRMAN: I remember once telling Mr. MacIntosh not to tempt fate.

Mr. PATON: The banks' endeavour is to remain closed for no longer than three days. Remember, we are subject to the federal labour code and other restrictive ordinances with which we have to conform. Perhaps Mr. Perry will



correct me if I am wrong, but on Christmas this year, for example, we will be open Saturday morning, and we will be closed Monday and Tuesday, following Christmas day.

The CHAIRMAN: If I could interrupt here, I think I must take the blame for allowing the Committee to stray away from the agenda before us. I am afraid I must take some of the blame for this because I assisted Mr. Lind in pursuing the topic. But I do think we have strayed from the subject before us, the banks' participation in other institutions. As I say, I apologize to the committee for encouraging this. I think we should return to the agenda.

We have Mr. Gilbert next, and he wishes to ask Mr. Cate some questions.

Mr. GILBERT: Mr. Chairman, I would direct Mr. Cate's attention to section 76(8) (C). Subsection (8) is the provision with regard to the diverting provisions applying to banks. Paragraph (C) reads:

a corporation engaging in the business of providing a service incidental or ancillary to, or used in the carrying on of, the business of the bank or of a corporation referred in clause (A) or (B) . . .

Mr. Cate, the first question I have is: Is "a service incidental or ancillary to", one and the same thing?

Mr. E. CATE, Q. C. (*Solicitor for The Canadian Bankers' Association*): There may not be very much difference, Mr. Gilbert.

Mr. GILBERT: On that assumption, would you give me a definition of those words "service incidental or ancillary to" the business of banking? What is contemplated by that term?

Mr. CATE: I thought, Mr. Gilbert, that this particular clause was intended to cover a situation such as this: You may have under (A) a corporation which is a subsidiary of a bank, owning bank premises which may belong partly to the bank and partly to someone else—a building which would be heated by a third corporation, or would be serviced in the way of building management and a number of things you could probably think of. I have read these clauses as having been put in with the intention of making it possible for a bank still to have more than a 10 per cent interest in a company of the kind I mention.

Mr. GILBERT: I wonder if I may be more specific and ask you directly: Do you think that this provision applies to RoyNat?

Mr. CATE: No, sir.

Mr. GILBERT: It does not?

Mr. CATE: I do not think so.

Mr. GILBERT: Does it apply to Kinross?

Mr. CATE: I am not familiar with Kinross, but I would expect the answer would be the same.

Mr. GILBERT: Therefore, in your mind this does not give RoyNat the opportunity to use this for their operations?

Mr. CATE: No, sir, it does not; not in my view.

Mr. GILBERT: Are there any other provisions that would apply to RoyNat that would give them the opportunity to continue?

Mr. CATE: Provisions that would enable that situation to continue?

Mr. GILBERT: Yes.

Mr. CATE: I think not.

Mr. GILBERT: You think not? You do not think RoyNat, which operates in mortgage financing, would be "a service incidental to" banking?

Mr. CATE: I would not think so, no. I would think it was part of banking. If the banks are going to be permitted to enter the mortgage business I would think it was part of the business of banking, and not something incidental or ancillary to it.

Mr. GILBERT: Therefore, you think that they would come under the general provision for "banking" of which mortgage is a part?

Mr. CATE: I would.

Mr. GILBERT: Let me ask you about some other companies that banks operate. Are you familiar with the Triarch Corporation.

Mr. CATE: I am afraid not.

Mr. GILBERT: You are not familiar with them?

Mr. CATE: No, I am not.

Mr. GILBERT: What about a company such as the one that is operated by the Bank of Nova Scotia, which operates in mortgage insurance?

Mr. CATE: I am afraid I am not familiar with that one either.

Mr. GILBERT: You are not familiar with it?

Mr. CATE: No; I think these are probably all companies which belong to individual banks and are known to them and their solicitors, but would not be known to me.

Mr. GILBERT: What about a company that operates a mutual fund?

Mr. CATE: I am afraid I have not come across that either, Mr. Gilbert. I do not know if there are any.

Mr. GILBERT: I had not either until I had done some research on it.

Mr. CATE: I did not know there were any. There may be; but I have not come across them. I do not know of any companies that do.

Mr. GILBERT: Are you familiar with the operations of the Mercantile Bank?

Mr. CATE: I am afraid not.

Mr. GILBERT: Perhaps I could direct my question then to Mr. Paton and Mr. Coleman and the other gentlemen.

Mr. Paton, what are your views with regard to the Triarch Corporation? I imagine you are familiar with Triarch.

Mr. PATON: I know the company, but I am not close to the operation. It is the Triarch Corporation of Toronto that you are referring to, I think.

Mr. GILBERT: Do you think this—

The CHAIRMAN: Could you identify this more fully for the Committee?

Mr. GILBERT: Yes; it is operated by the Canadian Imperial Bank of Commerce, and they engage in both equity and interim mortgage financing, Mr. Chairman.

These are part of the notes that were supplied by the Minister of Finance to the different members, Mr. Chairman.

The CHAIRMAN: Yes.

Mr. GILBERT: I was just wondering, Mr. Paton, if you knew how they would continue to operate? Would they operate under the banking provision, or would they operate under the provision which relates to "a service incidental or ancillary to"?

Mr. PATON: In general, I think my opinion of this bill is somewhat along the line taken by Mr. Cate, Mr. Gilbert. I hesitate to speak definitively about Triarch Corporation. You say that the Imperial Bank of Commerce has an interest in this company?

Mr. GILBERT: Yes, sir.

Mr. PATON: I do not know whether Mr. Sharwood would like to comment on that specific one, but, in general, in the area of the type of business that this company performs, I think we also feel that they would come under the clause that we are currently studying.

Mr. GILBERT: What about RoyNat, Mr. Coleman? How do you feel this fits in? Does it fit in under the mortgage clause?

Mr. COLEMAN: Do you mean, Mr. Gilbert, does it qualify for exception?

Mr. GILBERT: That is right.

Mr. COLEMAN: I do not take it that it does.

Mr. GILBERT: Do you feel the same about Kinross?

Mr. COLEMAN: Here, again, I am not familiar with Kinross, but I would think that it would not be far from RoyNat; although it is in a different type of business, as I understand it.

Mr. GILBERT: What about this other company operated by the Bank of Nova Scotia, which operates in the mortgage insurance field, Marlborough Properties?

Mr. COLEMAN: I would hesitate to speak on that, only because I am not familiar with it.

Mr. GILBERT: What about Toronto-Dominion's entry into mutual funds? I understand they have a 50 per cent participation in Corporate Investors (Marketing) Limited? How do they fit in, Mr. Paton?

Mr. PATON: That is in the marketing company, Mr. Gilbert. This is one of the services we felt we could usefully assist in providing.

I cannot give you a definite answer on how we feel about that particular corporation under this bill. We certainly have it under very close study.

Mr. GILBERT: Am I correct in assuming that in the trust companies, part of which are owned by the banks, the banks must divest themselves of their interest beyond 10 per cent?

Mr. PATON: That is our interpretation of the bill, yes.



Mr. GILBERT: What about the Mercantile Bank, Mr. Paton?

The CHAIRMAN: Mr. Gilbert, perhaps you could expand your question a little.

Mr. GILBERT: I am trying to draw Mr. Paton first.

Mr. PATON: Well, I hesitate to say that I am familiar with their operations.

The CHAIRMAN: The reason I interrupted was that, frankly, I found it a bit difficult to understand whether you were raising the question with relation to subclause 8(c)?

Mr. GILBERT: That is right. In other words, I understand that they also have a trust company.

Mr. ELDERKIN: No, Mr. Chairman, they do not.

Mr. GILBERT: All right, thank you. We are going to have someone here from the Mercantile Bank, are we, Mr. Chairman?

The CHAIRMAN: Yes; they have indicated that they wish to appear themselves, and they have filed a brief.

Mr. GILBERT: Mr. Paton, am I right in saying that you feel that RoyNat and Kinross do not qualify under any of the provisions of the Bank bill?

Mr. PATON: As an exception?

Mr. GILBERT: That is right.

Mr. PATON: I would say, in general, that our approach is that they would not qualify as exceptions. Whether we are right, or whether there is an area of discussion there—it would be very acceptable if we could find an area.

Mr. GILBERT: I think that is all, Mr. Chairman.

The CHAIRMAN: I will recognize Mr. Latulippe, followed by Mr. Munro.

*(Translation)*

Mr. LATULIPPE: Mr. Chairman, I have a question for Mr. Lavoie. I would like to know if the banks intend to use their finances for developments of natural resources. At the present time we are trying to develop our natural resources in Canada. They are not in the hands of the citizens because the citizens have to pay interest and taxes to government. By all sorts of ways they are diminishing the purchasing power of citizens. When it is the time to develop our natural resources in Canada there is no money left for the development of our natural resources and we are forced to expatriate ourselves, to tell Americans and citizens of other countries to come and develop our natural resources. They find it a pretty profitable undertaking, so these people come here and develop our own business, and here are the banks with all the economy of Canada in their hands and what are you doing to develop natural resources?

The CHAIRMAN: Mr. Latulippe, I will allow Mr. Lavoie to answer this particular question, but I feel I must interrupt you and tell you that we are not at the present time occupied with the investments of banks.

Mr. LATULIPPE: But I am concerned with the law of national resources.

Mr. LAVOIE: Mr. Latulippe, I know that certain banks have experts who are concerned with financing and with relations with companies engaged in development of national resources. It is a field of activity which is already covered by chartered banks. They are very interested in this field and they are giving considerable attention.

Mr. LATULIPPE: So far, they have not given this question very much attention, because 85 per cent of our natural resources are financed by foreigners. If you intend to do something new in the field, we would like to know what it is, because if this is not your intention, I think the government will have to do something to develop the natural resources by means different from the ones used in the past.

The CHAIRMAN: You would support the proposals of the bankers association that there should be no restriction on bank participation in our enterprises.

Mr. LATULIPPE: There is no restriction but there is no money left for the development of the natural resources, because all the governments are taking the citizens' money, all the governments, the school boards are taking the money away from the people, so there is nothing left for the development of the natural resources.

Mr. LAMBERT: Can I put a question to Mr. Latulippe? If you are trying to find money to invest in natural resources on a long term basis, how could you do that under the present Act, where the banks are not allowed to make long term investments. They cannot accept mortgages or some other securities. So, how can you claim the banks have the necessary power to engage in such long term investments?

Mr. LATULIPPE: I feel that the banks have had some power in this field. They, no doubt have found other more profitable fields of activities. The natural resources are the capital of the country, the real basis of the country. So, I maintain if you want to change the law, we will have to see that the banks take a greater interest than they have in the past in the financing of natural resources.

The CHAIRMAN: Would you like to propose something?

Mr. LAVOIE: The banks are always interested in helping new business to get going, but as Mr. Lambert has said, the banks would have no power to lend on long term. The concern here is short term loans. I am convinced that companies will come to banks for large short term loans if it is connected with natural resources development, I am convinced that the banks under such circumstances will lend to them.

*(English)*

The CHAIRMAN: Mr. Gilbert, I wonder if at this point you could clear up a slight mystery, if I may use that term. In the course of your questions, just before Mr. Latulippe began, you made reference to a list provided by the Minister of Finance. Is this something which you suggest has been presented to the committee, as such, or is it some other document?

Mr. GILBERT: It was sent to the members. It is dated October 7, Mr. Chairman. It is comprised of some notes on the revision of the banking system, together with press clippings. I was using one of the press clippings as the basis for my questions to Mr. Cate.

The CHAIRMAN: Yes; I just wanted to have that indicated, because, although I am not sure, I think these clippings were possibly circulated directly to all the members of the House, and were not presented formally by the Minister, or by someone on his behalf, to the Committee.

Mr. GILBERT: You are quite right.

The CHAIRMAN: I just wanted to have that cleared up to avoid possible misunderstanding later.

(Translation)

The CHAIRMAN: Have you concluded your questions, Mr. Latulippe?

Mr. LATULIPPE: Yes, for the moment.

(English)

Mr. MUNRO: Mr. Chairman, I understand that Mr. Fulton was pursuing this line earlier but I was not present. Getting around to this 10 per cent limitation that banks may have in any voting stock interest, I was wondering, in a very general way, without getting into the specifics of any particular companies in which you may hold stock, whether you can give us some general indication of the degree of participation by banks in equity stock of corporations other than corporations in related fields, such as banking and mortgage financing and so on? I am thinking more particularly of firms engaged manufacturing and in secondary manufacturing.

The CHAIRMAN: Do you wish to provide that information in a general way?

Mr. MUNRO: My understanding is that you have not suffered any limitation in terms of holding equity stock in such companies in the past. I wondered if you could give us some general idea of your activities in this field?

Mr. PATON: I do not know that I can completely, Mr. Munro. I think it would be reasonable to say that the banks' participation in corporations affected by this new section will be largely confined to financial institutions of one sort or another. There is no limitation on a bank investing in marketable shares of any corporation, and putting them into their investment portfolio.

Mr. MUNRO: But you indicated that you have not done it?

Mr. PATON: I beg your pardon?

Mr. MUNRO: Your activities have been largely in the fields related to banking rather than in the manufacturing and the secondary manufacturing fields?

Mr. PATON: I think that would be a fair statement, Mr. Coleman? Would you agree with me?

Mr. COLEMAN: I am not sure if Mr. Munro means have we bought shares in companies in the secondary manufacturing field?

Mr. MUNRO: Right; have you?

Mr. COLEMAN: I would think the banks' investment portfolio might have shares in different companies in Canada, but only from an investment standpoint.

Mr. MUNRO: Yes; I rather took it from Mr. Paton's general answer that there had not been any great activity on the part of banks in this area in the past.



Mr. COLEMAN: I would think that the activity except in special situations involving a substantial percentage—say, over 10 per cent—would be purely from an investment standpoint.

The CHAIRMAN: Portfolio?

Mr. COLEMAN: That is right.

Mr. MUNRO: You have indicated that you are less than enthusiastic about this 10 per cent limitation. You make some noteworthy statements on pages 11 and 12 about what you would do if this limitation were removed. Have you any intention, along these lines, of increasing your participation in equity ownership in the manufacturing field in Canada? I am referring to statements such as the one where you talk about the expanding enterprises in Canada and your desire to participate in them. This is the general tone of your remarks. I wondered if you had that in mind were this limitation removed?

Mr. PATON: I think our reference here, Mr. Munro, would be that we would desire freedom to bring into being, or participate in, developments to further the financing of trade commerce and exports and so on, in the Canadian economy, remembering at all times that we are essentially in the banking and—to use Mr. Gilbert's reference—"ancillary" businesses.

Mr. MUNRO: You really do not regard it as part of your function to fulfill your role in the financing of Canadian corporations?

Mr. PATON: That is our main function, actually.

Mr. MUNRO: I mean in the secondary manufacturing field.

Mr. PATON: We are substantially involved in the financing of these groups of industry that you refer to, and we will always continue to be.

Mr. MUNRO: But not in terms of ownership.

Mr. PATON: Equity ownership?

Mr. MUNRO: Yes.

Mr. PATON: Our interest, perhaps, will be in capital financing under the new provisions.

Mr. MUNRO: What about your role in equity ownership of these corporations rather than in the long term financing which Mr. Lambert has referred to? What are your views on active participation in terms of equity ownership of stock?

Mr. PATON: I do not think that we have plans or ambitions to develop along the lines you suggest.

Mr. MUNRO: Would this general theme of lack of intent in this area of equity ownership in stock apply also to the natural resources of this country, in terms of companies designed to develop Canadian natural resources?

Mr. PATON: I think the answer to that is that we would be very anxious to participate in the development of natural resources but not essentially on an equity basis. I certainly would not want to imply at all that we would be hesitant about going into this type of financing, in a normal banking way but in so far as anticipating that a major part of our operation would be in equity participation.

Mr. MUNRO: In terms of voting stock, what are your feelings?

Mr. PATON: I think our intention would be to continue somewhat along the lines we have followed in the past.

Mr. MUNRO: And past practice has certainly not indicated that there is a behavioural pattern on the part of the banks in this area?

Mr. COLEMAN: I do not think we would go into an equity ownership position to the extent that we would be attempting to influence management. As I said before, it would be purely if we thought it was a good investment, and, at that same time, thought that a reasonably small holding was perhaps helping out that area of the economy.

Mr. MUNRO: Would there be any tendency to think more along these lines if the limitation were removed?

Mr. COLEMAN: I would think not, speaking for our bank. I do not think we would want to own drug stores and woollen mills and things like that. I think we would want to stick to the banking business and matters relating to the general financial area. I think that type of companies that the banks have any important interest in shows that we have stuck purely to companies in the financial business.

Mr. MUNRO: Is there any reason to suggest that equity ownership in these companies is not a relatively lucrative area for participation?

Mr. COLEMAN: I would say that it is not the proper function of a bank. I think that, from the standpoint of prudent investment, you would want to have diversified investment portfolio, without having too much in any one area; unless it was something that you were knowledgeable about and could direct.

Mr. MUNRO: I agree with that contention. I am merely suggesting that because it is equity ownership does not necessarily mean that it is not a responsible investment.

Mr. COLEMAN: Oh, I agree completely.

Mr. PATON: We would probably have to be careful that we were not getting into an area of conflict of interest, where we were shareholders and also, quite possibly, a major creditor through financing under our normal banking operations.

Mr. MUNRO: This is a thing about which you have not been too worried so far as trust companies and so on are concerned.

Mr. PATON: We are not a major creditor at all, in these instances, Mr. Munro. In fact, it would be safe to say we are not a creditor at all.

Mr. MUNRO: But you have ownership in them?

Mr. PATON: Correct.

Mr. MUNRO: And the same thing exists, I am suggesting, in these other areas in which you indicate a reluctance to participate on the basis of conflict of interest.

Mr. PATON: The need for us in the areas you are covering is as a financial intermediary to provide working capital to enable them to perform their func-

tion and expand. The other area, we referred to covered trust companies and other institutions not entirely dissimilar to our own operations.

Mr. MUNRO: You will certainly be well aware of the discussion there has been in this country for some time about the degree of foreign ownership and control in some of these areas. It is difficult to see how this situation can be improved if there is not more active interest by institutions such as your own.

Mr. PATON: I could quote you one specific instance in our own institution where, by participating in a corporation, we were responsible for repatriating the majority ownership of it back into Canadian hands; and that investment company has also successfully repatriated ownership of companies it has financed.

Mr. MUNRO: That is encouraging.

That is all, Mr. Chairman.

The CHAIRMAN: Thank you. Mr. Johnston, did you signify that you had a question?

Mr. JOHNSTON: Yes; we are getting very close to the question I wanted to ask regarding the disposition of a company. We have heard about a total lack of loyalty as far as money is concerned, and I was wondering whether the banks have any policy in their voting rights regarding Canadian ownership of companies, or whether there was a tendency to let the company go to the best offer without giving any consideration to that factor.

You have mentioned this. Would you like to elaborate on it? You were talking about repatriating and you were giving instances but actually you were working in the opposite direction. I suppose at times there are instances where it operates in the opposite direction, as well?

Mr. PATON: I am not aware of any bank that has the ability through share ownership to direct the sale of such a corporation. I think this is your question, Mr. Johnston.

Mr. JOHNSTON: Yes.

Mr. PATON: Presuming a bank had a substantial ownership in a company?

Mr. JOHNSTON: Yes.

Mr. PATON: I could not answer your question without actual knowledge, and I have no knowledge that such a situation exists.

Mr. JOHNSTON: Can you tell the Committee what is the prime reason for these limitations to which you object?

Mr. PATON: I think perhaps I might refer to the Porter report again. My recollection is that the commissioners chided the banks for having been somewhat less than imaginative—in fact, perhaps they used the word “unimaginative”; but when they were comparing the relative growth of the near-banks with the banks I think they indicated that this was not altogether the result of aggressive action by the near-banks, but that perhaps the chartered banks could have been a little more aggressive. I think that we have here an area where we have been quite aggressive, and our pursuit of this aggressiveness is, perhaps, going to be interfered with. That is one reason for our objection.



Mr. FULTON: I think Mr. Johnston's question was the other way around. I believe he was asking why do you suppose the government is objecting to your continuing this?

Mr. PATON: I thought you were asking me what exceptions I take to—

Mr. JOHNSTON: No, no. I was asking if you would care to hazard any guesses about what the government thinking was?

Mr. PATON: No, sir; I certainly would not. I could have saved some time if I had interpreted your question properly. I am sorry.

Mr. JOHNSTON: Thank you.

Mr. MUNRO: Mr. Chairman, just to pursue this a little further: In terms of direct participation in equity ownership in the manufacturing, secondary manufacturing, and natural resource fields, even if this limitation were lifted your financing would not be in this type of direct participation?

Mr. PATON: Not in our present thinking, Mr. Munro.

The CHAIRMAN: Are you finished, Mr. Munro? Mr. Latulippe?

(Translation)

The CHAIRMAN: Mr. Latulippe?

Mr. LATULIPPE: I would like to talk about the financing of public affairs.

The CHAIRMAN: Mr. Latulippe, I am sorry to interrupt you, even before you ask your questions, but I have already indicated that in my opinion, perhaps I am wrong, but the financing of public affairs has nothing to do with the restrictions of banks or other companies, that is to say private companies.

Mr. LATULIPPE: But what about the investments of banks in public affairs, when they lend money to provinces, to municipalities?

The CHAIRMAN: It is a very important matter, but at the present moment, we are not discussing in any way the investments of banks in more or less public corporations, for example, municipal corporations, the investments of banks in private companies, in loan companies, mortgage companies, that does not concern us here.

Mr. LATULIPPE: That does not include public matters such as in the provinces?

The CHAIRMAN: No. I may be wrong, but the chairman has to give rulings.

Mr. LATULIPPE: So we will have special discussions on that—

The CHAIRMAN: I suggest when we conclude our discussions on this part, there will be some particular points, we will have some time for general discussion.

Mr. LATULIPPE: It is not a general discussion.

The CHAIRMAN: What I mean is that it could include your question.

(English)

I would suggest that questions be limited to this area, if there are any further questions.

If not, we should move on to the—

Mr. MUNRO: Mr. Chairman, may I be permitted just one more question on this line.

Mr. Paton, can you imagine, or envisage, any type of governmental inducements or policies that would act upon the banks in a way that would encourage them in this type of direct participation that I have been talking about?

Mr. PATON: I really do not think I could, Mr. Munro. I feel that the opportunity to do what we have been doing, and to expand in that area, would be very acceptable to the banks and would be sufficiently inclusive to enable us to do the job that we would like to do.

The CHAIRMAN: The next topic is "Disclosure of Accumulated Appropriations for Losses on Loans and Investments." This is a rather fancy way of talking about the disclosure of so-called inner reserves, if I may summarize the topic in that way.

Have you a question, Mr. Clermont, or did I misunderstand your gesture?

Mr. CLERMONT: I wonder if I might be allowed to be first at eight o'clock, because I cannot stay at the moment.

The CHAIRMAN: I see; you have to go to another meeting at this time.

I will recognize Mr. Lambert.

Mr. CLERMONT: I am sorry, Mr. Chairman, but will I be able to start at eight o'clock, because I will have to leave at around twenty minutes to nine?

The CHAIRMAN: I understand your position.

Mr. CLERMONT: Perhaps I am asking a special favour, but I am one of the regular members. I do not think I miss many sessions—

The CHAIRMAN: Yes, you are a regular member. You are a very active member, and making a distinguished contribution to our work, if I may say so.

Mr. CLERMONT: It looks as though we may not see these gentlemen for a while after tonight.

The CHAIRMAN: Oh, no; they have indicated that they are going to pay very close attention to our proceedings.

Mr. CLERMONT: No; I am talking about them as witnesses. I am sure they will be at the back.

The CHAIRMAN: Just for the record, perhaps, you are referring to that part of the room reserved for the general public.

I am sure the committee would accord you the courtesy of placing your questions at eight o'clock.

Mr. CLERMONT: Thank you very much.

The CHAIRMAN: In that case I will recognize Mr. Lambert.

Mr. LAMBERT: I will be brief.

I find myself at some disadvantage with regard to this, because we were not able to get from Mr. Elderkin—and quite properly so—the policy reasons for this change. I always work on the assumption that he who proposes the change must

justify the change. Unfortunately, we have not had the Minister of Finance here so I feel as though I am doing a little shadow boxing.

I cannot see the purpose of this as a matter of fact, but, having said that—and we discussed this the other day—will there be very much prejudice to the banks if they publish these inner reserves? They already disclose them to the Minister of Finance, so therefore they are not a deep, dark secret. To what extent do you feel that the banks' positions would be prejudiced as a result of this requirement? This is somewhat like defending yourself against something on which there has been no charge.

Mr. PATON: Mr. Lambert, I feel, basically, and very definitely, that the situation we have at present has been well justified over many, many years. I feel that perhaps the buoyancy of conditions over the past 20 years, perhaps, might have dulled the sensitivity or the memories of people in that we cannot be assured of a continuation of such times, and if it was in the past fully justified that disclosure be not permitted it is very difficult for me to see where there should be any change. The reasons in the past would be equally prevalent and equally important under present conditions.

We have outlined two main reasons in our brief that public disclosure of the banks' complete reserves, both on an annual operating basis under "O" and a full disclosure under "P" in the schedules that we have, could be an embarrassment under certain economic conditions. Companies do not fail on averages but have a habit of failing at one time, perhaps. I am speaking generally. Your reserves must always be more than ample to meet the contingencies of this situation, and even if they are more than ample, the impact on them at any one time under certain conditions might be quite severe and the publication of this impact could have a detrimental effect on public confidence. It also might happen that one particular bank might have unfortunate experiences, and not only could public confidence be impaired in them it might apply to the general banking community at a time when it would be unfortunate for it to do so. Any time would be unfortunate, but some times can be more unfortunate than others, depending on conditions.

The other main point is that banking is a risk business and calls for a lot of experience, anticipation and a certain amount of hope, too. If it were a fact that complete disclosure was in effect it could inhibit the credit judgment of bank management. In other words they might not be prepared to go quite as far in the financing operations as they do under the present situation.

Mr. LAMBERT: Mr. Paton, I do not know whether you are familiar with major trust company operations, but can you tell us whether major trust companies do include inner reserves?

Mr. PATON: They have a reserve formula, the details of which I do not have. It is something, I think, that we could get.

Mr. ELDERKIN: It is 3 per cent, Mr. Chairman, on mortgages.

Mr. LAMBERT: Mr. Elderkin, as far as you are aware, there is no similar provision with regard to the federally incorporated trust in that they maintain inner reserves, as well?

Mr. ELDERKIN: Well, this is a 3 per cent inner reserve, in effect, which is not disclosed from the trust companies.



Mr. LAMBERT: I see. The trust company, then, would not have to disclose if it had any losses, as is proposed in this bill?

Mr. ELDERKIN: I think not. I am really not competent to answer that question.

Mr. LAMBERT: Perhaps, Mr. Chairman, we could have our research staff look into this question of whether trust companies at the present time do maintain inner reserves, as indicated by Mr. Elderkin, and if they must make a disclosure as would be required by the Bank Act.

The CHAIRMAN: I think that would be a very useful question.

Mr. LAMBERT: If it is a question of competition, then I would suggest, if it is not applicable to the trust companies, that this is particular discrimination against the banks.

The CHAIRMAN: Perhaps I could mention at this time that Professor Baribeau has prepared a report entitled "Number of New Housing Units Financed Through N.H.A. Mortgage Loans by Type of Lender and Areas for the Year 1959", in response to a question Mr. Lind asked. Miss Ballantyne has made copies of this and I would like to have them distributed.

I think, Mr. Baribeau, there was a very brief explanatory comment that you wanted to make?

I might say, in passing that I understand that the Porter Commission did recommend the disclosure called for by the bill.

*(Translation)*

Mr. BARIBEAU: I think the question just asked by Mr. Clermont was intended to point out how the chartered banks could serve small communities as so far as concerns loans guaranteed under the National Housing Act. Well, I went and I got certain figures from C.M.H.C. regarding loans granted in various areas and the regions, grouped in accordance with the 1961 census into metropolitan regions and principal urban regions with a population over 5,000 and other regions.

The chartered—I could not get any information about the value of loans approved under the National Housing Act,—but I did get a number of units of residential housing units, built and financed under the various sections of the National Housing Act, through different kinds of lenders.

The chartered banks—I could not get figures for any other period than 1959. That's the only year for which you can get them. So, in 1959, the chartered banks financed 14,844 housing units, 58.2 per cent of houses financed by the chartered banks under the National Housing Act were financed in metropolitan regions.

So far as other approved lenders are concerned, they lent 74.7 per cent in metropolitan regions, so on the basis of these figures I conclude that the chartered banks lent more than the other approved lenders did in non metropolitan areas, in non metropolitan centres.

Now, if we take centres with a population of 5,000 and more, going up to 50,000, we see approximately 12.2 per cent for the banks and 6.9 per cent for other approved members.

The CHAIRMAN: Thank you, Mr. Baribeau.

*Editor's note: The chart tabled by Mr. Baribeau is as follows:*

NUMBER OF NEW HOUSING UNITS FINANCED THROUGH NHA MORTGAGE LOANS  
BY TYPE OF LENDER AND AREAS FOR THE YEAR 1959\*

Lenders	Metropolitan areas	Major urban areas	Centres of population 5,000 and over	Other areas	Total
Chartered banks.....	8,645	1,922	1,811	2,466	14,844
—percent distribution.....	58.2	13.0	12.2	16.6	100.0
Other approved lenders.....	8,849	1,421	811	760	11,841
—percent distribution.....	74.7	12.0	6.9	6.4	100.0
All approved lenders.....	17,494	3,343	2,622	3,226	26,685
—percent distribution.....	65.6	12.4	9.8	12.1	100.0

\*SOURCE: CMHC—Data for other years not available. Areas are defined according to the 1961 Census.

(English)

May I have a motion that the table that has just been distributed be incorporated in our record?

Mr. FULTON: Could we not have it incorporated in yesterday's record where it would be closer to the question?

The CHAIRMAN: Yes; I think that is a good idea. Perhaps you would make a suggestion on where we should put Mr. Baribeau's explanatory comments?

Anyhow the committee agrees that the table be incorporated in the appropriate part of the minutes.

Before we recess I should clarify something I said previously. I said that the Porter Report recommended the disclosure of inner reserves. What I should have said is that Porter report stated: "It is our view that there is no compelling case against disclosure, and we are satisfied to leave the matter in the hands of the authorities and the shareholders concerned". I thought I should mention that because by initial comment, I think, conveyed the wrong impression.

Mr. LAMBERT: Mr. Chairman, I regret that I will not be able to be here this evening. I know that the bankers' association have one of their men here in regard to one question that I would ask when we have completed the paper. My question has to do with the use of computers in banks and how their use may affect the branch banking system. This is something new, and I have discussed it with a number of representatives of the banks. They have some very interesting information with regard to this, and I think it would be very useful for the committee to have some comment, perhaps *in extenso*, on the future of computers and on their effect on the branch banking system, since we are going to be dealing with the period of the next ten years.

The CHAIRMAN: I will note your suggestion.

(Translation)

Mr. LATULIPPE: Would it be possible to have French interpretation I have not understood a word.

(English)

The CHAIRMAN: We have a certain difficulty which was brought to my attention rather late in our proceedings this afternoon. There is a problem with the interpretation staff today. Several of them are off through illness and the remaining staff has to cover the House of Commons, the federal-provincial meeting and the various committees. I apologize to the committee for this problem. I had not realized its seriousness and I am sorry that it was not brought to my attention earlier. Because nothing was said I assumed that the translation was adequate. We will try to bring about an improvement.

The meeting is adjourned until eight o'clock this evening.

#### EVENING SITTING

The CHAIRMAN: Gentlemen as we are resuming the meeting that recessed at six o'clock. I think it would be appropriate to recognize Mr. Clermont. Now Mr. Clermont we agreed to hear you this evening.

Mr. CLERMONT: I do not think there is much choice with the number of members present.

The CHAIRMAN: Let us say for the record the number is sufficient for our purpose.

(Translation)

Mr. CLERMONT: Mr. Chairman, I will direct my first question to Mr. Lavoie. I believe that this evening we shall deal with the matter of internal reserves? This is my first question to Mr. Lavoie in this regard. How many types of internal reserves are there of general character?

Mr. LAVOIE: There are internal reserves of general character, there are internal reserves on which you pay taxes and on which the tax has not been paid.

Mr. CLERMONT: In the Porter Commission report mention is made of general internal reserves and specific internal reserves. What are these specific reserves? Are these reserves in respect of which taxes have been paid, or is it another type altogether?

Mr. LAVOIE: The specific reserves are the reserves which are allowed on investments and loans, but these are non-current.

Mr. CLERMONT: Chartered banks, collectively and individually, apparently object to Clause 60 of Bill C-222 with regard to making public knowledge of the internal reserves. You point to the fact that this might bring about some misgivings of the shareholders or the people if there were higher than average losses over one year, in loans or investments. However, I am told, and I think that I am right, that large United States banks have to make that knowledge available to the public and as far as I know this has never hurt the reputation of American banks.

Mr. LAVOIE: Mr. Clermont, I believe the United States banks are not all obliged to declare what their internal reserves are, nor must they declare the



losses they have suffered. There are certain banks which do make public these financial statements and in whose financial statements are the sum of their debts.

Mr. CLERMONT: Am I right in saying that certain larger American banks have to reveal their internal reserves?

Mr. LAVOIE: If I am properly informed, Mr. Clermont, I do not think that the banks are obliged to make this known, I think they make it known on a voluntary basis.

Mr. CLERMONT: But that is the version, of course, of the representatives of the chartered banks association. On the other hand, we have the evidence of a great many other people who are experts in this particular area. These people claim that to make these reserves public knowledge, would be such as to give more information about the shareholders of the banks, and actual assets.

Mr. LAVOIE: Mr. Clermont, there is a goal in maintaining these inner reserves. The main purpose of maintaining these inner reserves, is to meet the losses the banks might suffer, or one bank in particular might suffer over the course of a year. If these reserves are made public and, for instance, that same year a bank was to suffer very heavy losses, I think it would not be wise from the viewpoint of public confidence in the bank, and certain depositors indeed, might feel their deposits insecure if such losses were made public, even if the losses were only once during any given period.

Mr. CLERMONT: But Mr. Lavoie, does not Bill C-222 once enacted by Parliament, prevent chartered banks having hidden internal reserves which would not be public knowledge.

Mr. LAVOIE: Oh, yes, there is always a reserve. But if you ask us to reveal the extent of it, you will be asking us to reveal our losses during the last five years, we will have to reveal everything in regard to losses and surpluses.

Mr. CLERMONT: To return to the subject. If for any particular year, chartered banks were required to reveal losses which would be larger than the previous year, or the two previous years, could this give rise to a loss of public confidence.

Mr. LAVOIE: The Bill as submitted to us here indicates there will be a period of five years to establish the average of losses that we shall have suffered. I believe that using this average, without revealing all the internal reserves of the bank, would give the public a pretty good idea as to the profits, the true profits of the chartered banks.

Mr. CLERMONT: But to return again to your claim that this might bring about some misgivings among the people if you were to make this knowledge public. If the bank had suffered a greater loss than usual, do you not feel, Mr. Lavoie, that the possibility of a deposit insurance featured in this Bill, or elsewhere not important in the public mind, even if banks were required to publish these reserves? Even if the losses for one year were greater than for another?

Mr. LAVOIE: It is difficult for me to express an opinion with regard to the proposed insured deposits, because this Bill has not been passed yet.

Mr. CLERMONT: No, but all M.P.'s are aware of it.

Mr. LAVOIE: What is done in companies is this. Companies can create reserves on their inventory and even on accounts receivable, and they do not have to publish figures and I do not see why in the banking system, we could not have reserves in the same way, if it would enable us to face eventual losses.

Mr. CLERMONT: If I put that question to you it is because there is nothing in this Bill now before the House which would prevent the banks from establishing a hidden internal reserve provided taxes had been paid in respect of that reserve.

Mr. LAVOIE: We do have reserves, internal reserves, shares that are not made public and the tax has been paid on these sums. This does exist in the banking system now.

(English)

Mr. CLERMONT: Mr. Chairman, I will direct this question to Mr. Paton. According to the annual reports of seven banks out of eight for October 1965, capital paid up was \$285,958,000; the rest account was \$936 million; undivided profits, \$13,361,000. Now, Mr. Paton, out of the \$13,361,000 one bank had the amount of \$6,079,000 as undivided profits. Is it possible to know the reason why it is so big an amount compared with the others, because the total undivided profits for seven banks out of eight as of October 31, 1965 was \$13,361,000 and one bank, and you know that bank, has undivided profits of \$6,079,000?

Mr. PATON: There is nothing mysterious about that, Mr. Clermont. It is purely a management decision.

Mr. CLERMONT: I did not intimate there was anything mysterious.

Mr. PATON: Undivided profits are purely a management decision.

Mr. CLERMONT: Mr. Chairman, perhaps I will be allowed to ask one question that I asked Mr. Elderkin when he was a witness before this committee. He said when the bankers' association are here as witnesses I may ask this question. Here is my question and it is with regard to the shareholders' equity, the number of shareholders. As it is now we have a report that shows so many shares up to 500 shares, 500 shares to 1,000 shares and 1,000 shares and over. Would it not be possible, Mr. Paton, that instead of less than 500, it should be less than 100, and also 100 to 400. I think it will give a better picture of the shareholdings.

Mr. ELDERKIN: Mr. Clermont, perhaps I could help on that question. The present act provides that the banks are only required to report holdings of 500 shares or over.

Mr. CLERMONT: If we want the information it will be up to us to propose an amendment to the present law?

Mr. ELDERKIN: We would have to go back to the banks to find the breakdown of the shareholders under 500 shares. We do not receive that information at the present time.

Mr. CLERMONT: I know, you told me you received this report from the banks, but I mention to you also that amongst the reports that you gave to this committee there was one showing the breakdown of deposits and it had the number of deposits from \$1 to \$100. I am sure it is much more worthwhile to find the answer to that than to find the number of shareholders, because according to

the last report I think there were 118,413 shareholders throughout the eight chartered banks. It is only a suggestion, but according to Mr. Elderkin the present law would have to be changed in order to do this.

Mr. ELDERKIN: No, Mr. Clermont, the present law does not have to be changed because the minister has the authority to call for any information he requires. The act only requires the present authority.

Mr. CLERMONT: Thank you, Mr. Chairman.

Mr. FULTON: Mr. Chairman, I really have no questions on the rest accounts. But I wonder if I could ask a question now, on a matter which is not covered in the brief. I ask permission now because the Department of Finance estimates are before the House and are to be followed by Mines and Technical Surveys and I should like to be there—

The CHAIRMAN: You could comment on those. I think the committee will be happy to accord you that courtesy.

Mr. FULTON: I should like to ask Mr. Paton if he would comment on a matter that was raised when Mr. Elderkin was the witness. It is the question of requiring the banks to register section 88 security in the central registries of provinces which have central registries. Would this be an onerous thing, something to which you would object?

Mr. PATON: I think we would prefer Mr. Fulton, not to open up the registration requirement of section 88 security. As you know, we presently register these in the Bank of Canada offices in the respective jurisdictions. I was here, I think, when you were discussing this with Mr. Elderkin and at that time we were very largely concerned with the question of registering chattel mortgages in a central registry office. In that area, of course, the banks would be very happy and pleased to co-operate. But I think I speak on behalf of the association when I say we would prefer not to have the additional onus of registering section 88 security (a) with the Bank of Canada office plus (b) with the central registry office.

Mr. FULTON: Why? It would only be one other piece of paper, would it not?

Mr. PATON: Possibly in the clerical work it might not be extensive, but to have it officially written into section 88 would impose the liability on the banks to protect their security by complying with this additional registration feature. It is not an impossible thing for us to do but if you asked me if we had any objection I would say our preference would be to not do so.

Mr. FULTON: I can understand. No one wants to have their burdens increased but you cannot really tell me that it would be an onerous burden?

Mr. PATON: You mean from a work or a time standpoint?

Mr. FULTON: Yes.

Mr. PATON: No, I cannot say that. I agree.

Mr. FULTON: That is all, Mr. Chairman.

The CHAIRMAN: Thank you, Mr. Fulton. I wonder Mr. Paton, if I might deal with one or two aspects of this question of inner reserves. I gather the position of the bankers' association, as you have pointed out here, is that one strong argu-



ment for continuance of the present practice is that it helps to maintain the confidence of the public, and so on. Are you aware of the fact that the Porter Commission has taken a somewhat opposite view on that specific argument? At page 388 they say:

On the other hand, the views of informed observers and the experience of other financial institutions in Canada and abroad could be cited just as easily to support the opposite viewpoint that rumours can be more dangerous than facts, and that the public is well enough informed to accept occasional severe losses as a normal part of any banking business, that the shareholders are entitled to know how their company and its management are performing, and, finally, that the discipline of public disclosure is good for management.

They they go on to say what I quoted before we adjourned for supper. Would you not feel there is something to be said for this opposite argument as well, which might be to your benefit as much as anyone else? I might be putting you in an unfair position by asking you to reply to the question the way I put it, and perhaps I should expand the question. It would appear to me that the existence of these inner reserves makes it possible for a lot of misconceptions to arise in the public mind. The very term "inner reserve" has a certain connotation of secrecy, of something being kept away, and so on. It could be argued, could it not, that the maintenance of this concept, whether you call them inner reserves or hidden reserves, or whatever term is most—

Mr. PATON: Contingency is a nice word.

The CHAIRMAN: Yes, contingency reserve. The way in which they are being kept now helps to maintain a rather inaccurate impression in the mind of the public as to what you people are up to?

Mr. PATON: I would not argue, Mr. Chairman, that there is no substance to the other side of the argument as expressed by the Porter Commission. There is a certain amount of conjecture in their statement. No one knows just what the public reaction would be if the situation we previously described ever came up. Rather than incur the potential risk of an adverse reaction, in our deliberations we have failed to see the advantage in changing a system that has worked very well and that has permitted, we think, reasonable disclosure of the banks' operations from year to year and has contributed, I would say, to a record that is quite outstanding in the world as far as any banking system is concerned. In short, when things are going very well and there is no real justification for changing the *modus operandi*, we are better to continue as we are.

The CHAIRMAN: That does not seem like the comment of a forward-looking and competitive-minded industry.

Mr. PATON: Perhaps my main concern is that we continue to have that image.

The CHAIRMAN: I would think, Mr. Paton, if I may say so, with respect to the opinion of the public or the image in the mind of the public of the banks, the key factor is the view—which may not be expressly found in the legislation as yet—that the government will not permit the banks to get into any difficulty which would be to the detriment of the public interest.

Mr. PATON: I would strongly object to any thought that current management and future management of any of the banks would proceed with their daily operations on the basis that no matter what their judgment is, they are going to be bailed out in the event of problems. I think this would be a very unfortunate philosophy to enter into any of our thinking.

The CHAIRMAN: It would be an unfortunate philosophy to enter into your thinking as bank management, but I am just suggesting in the mind of public, perhaps conditioned by what they know of the United States system, the fact of potential government support is an important item that influences their thinking. The reason I say this is I was very impressed by something you said in a speech you gave to the Canadian club on November 7. It was a very interesting and informative speech. The only serious criticism I may have is that some of your flashes of humour are not found in the written text. I say this because reports have reached me that the humour did work its way into the remarks. On page 10 you say:

The chartered banks do not need deposit insurance. They are already subject to close inspection and supervision and their ability to meet their deposit liabilities is undoubted.

Then you go on to say:

The most effective guarantee of the safety of deposits is sound financial management, and in this connection I would remind you that for more than 40 years there has never been any serious concern about the safety of deposits in Canadian banks.

Of course, if you look back about 40 years, that is about the time the office of the Inspector General of Banking was created. As I say, I wanted to read this into the record because I found it a most impressive comment. If the committee would permit me, I would like to ask you one or two other things about your arguments on behalf of the present system of inner reserves.

You were kind enough to table before the committee a document headed "Some Brief Comments on the Profitability of the Canadian Banking Industry" and you have given certain figures showing your profit position compared to other industries, including financial institutions. Without getting into the figures at this moment, could you tell me to what extent or how the profit figures contained in this document reflect the hidden reserves?

Mr. PATON: They do not reflect the contingency reserves at all, Mr. Chairman. These profits are the reported profits of the bank after provision for the reserves.

The CHAIRMAN: Does this mean that if the contingency reserves are taken into account your profits would actually be higher?

Mr. PATON: If there was no provision for reserves from a year's operations, then the actual earnings would be shown on a higher basis.

The CHAIRMAN: Without at the moment entering into an argument on the need to maintain contingency reserves, it could be that if they were taken into account your position in comparison with the other industries in this schedule would be somewhat more favourable than the schedule shows?

Mr. PATON: Correct, assuming that there are no reserves in the earnings shown by these other industries, and this is a point that Mr. Lavoie made earlier.

These other industries do have reserve features in their statements; inventory reserves, receivable reserves, which are—

The CHAIRMAN: Which are reflected in their statements.

Mr. PATON: No, sir. The inventory is normally shown as a net figure, and receivables likewise.

The CHAIRMAN: Do not balance sheet statements often have such things as a reserve for bad debts, and so on?

Mr. PATON: Your published statements, Mr. Chairman, I think in the main do not show them. Your published statements show a net figure for receivables.

The CHAIRMAN: Let me pass on to another point that interested me. On page 15 of of your brief you say:

No other commercial or industrial company is placed in the position of being required to reveal annually the amount of losses suffered on . . . products, development of new products which fail, bad debts, etc. since these are considered to arise from normal business activities.

Now, perhaps Mr. Elderkin could help us in this, but are you suggesting that the proposals of the Bank Act would force you to show that you have a certain bad debt loss in retailing and a certain bad debt loss in farming, and so on and so forth?

Mr. PATON: Oh no. The provision here would require disclosure of losses as a total and as prescribed in forms "O" and "P", which rather complicates it.

The CHAIRMAN: We saw these some weeks ago and I am not going to attempt to dig them out. In that case it would seem to me you are not too much different from a commercial or industrial company. You are not asked to particularize the nature of your losses in the sense of saying "But we lost so much on loans to retail grocery stores and so much on loans to spinning mills", and so on.

Mr. PATON: That is correct, but we are being asked to disclose our total losses under the prescribed forms, whereas in the case of commercial or industrial companies they do not show the loss total at all. The losses derived from these various operations, such as the development of new products, would go into their cost.

The CHAIRMAN: It would go into the profit and loss statement if they had a net loss on the year's operations. That is shown.

Mr. PATON: The net figure is shown but the cause of that loss, Mr. Chairman, is included in the global figure, cost of goods or cost of manufacturing.

The CHAIRMAN: The reason I draw this to your attention is that someone reading this quickly might get the impression that you have to disclose your loss on a loan to develop a new product, or on a loan of a particular category of industry, and so on, which you will agree is not the case?

Mr. PATON: That is right.

(Translation)

The CHAIRMAN: Mr. Latulippe?



Mr. LATULIPPE: I would like to put a fairly direct question, how do these internal reserves compare with your general reserves?

Mr. LAVOIE: Mr. Latulippe these reserves are set on a percentage, set to a percentage, a total percentage of our loans and this percentage varies from year to year and is given to us by the Inspector general of the banks.

Mr. LATULIPPE: Is there any particular reason why you should not indicate to the public what your internal reserves are, when the public can find out what the general reserves are?

Mr. LAVOIE: I think, Mr. Latulippe, that I already replied to this question some minutes ago, when I replied to the question put by Mr. Clermont. One thing is certain, if the banks must divulge the losses that they have suffered each year on their loans, they will obviously be a good deal more prudent in the operations they will conduct and probably will take much less risks than they do at the present time.

Mr. LATULIPPE: According to our information, your losses are not considerable, they are not even 1 per cent, why then make such difficulties when your losses are no higher than they are? Do you say that you have higher losses than that?

Mr. LAVOIE: It is rather difficult to answer your question and to tell you exactly what will happen over the course of the next few years. One thing is certain that the reserves that we maintain against the eventuality of loss are not out of proportion to the losses which the banks do suffer over the course of the years.

Mr. LATULIPPE: You have transferred several million dollars from general reserves to internal reserves, is that a fact? You did transfer fairly considerable sums of money in this way?

Mr. LAVOIE: That could happen, yes, over the course of a year. A bank will decide to transfer to its internal reserves sums from its current reserves, this is done quite currently, this is quite usual, it is up to management or the bank administration to decide what amount each year will be taken out of internal reserves and transferred to the reserves that are given in the financial statement.

Mr. LATULIPPE: Could you tell me if this is indicated in the annual report, where is this figure found? Is it there at all?

Mr. LAVOIE: If a bank, over the course of a year, transfers internal reserves, some of its internal reserves to its ordinary reserves, this is indicated in the financial statement at the end of the year, that is at the end of the financial year and when the financial statement is made public.

Mr. LATULIPPE: Thank you, Mr. Chairman.

The CHAIRMAN: Mr. Caouette, if you please.

Mr. CAOUCETTE: Mr. Lavoie, you have been speaking here of losses sustained by the banks, you have been speaking too of internal reserves as well as general reserves. Now, let us assume that a bank is in difficulties, let us assume that it has suffered considerable losses, through some operations of the Bank of Canada buying a Government bond or security, would this enable the bank to reestablish its financial position; it will of course lose money, but could it not consolidate its position nonetheless?

Mr. LAVOIE: Mr. Caouette, when a bank suffers a loss, it has no alternative but to charge it against reserves.

Mr. CAOINETTE: Yes, I understand that, but I have just come from the House and I put a question to the Minister of Finance, in fact, we will meet him here. If the Bank of Canada were to buy a Government security in the amount of 1 million dollars, this is added to the reserves of the entire chartered bank system, is that a fact? You do not have to deposit anything, simply the purchase by the Bank of Canada of 1 million in Government securities will add to your reserves, do you agree?

Mr. LAVOIE: The money reserve?

Mr. CAOINETTE: Pardon?

Mr. LAVOIE: The money reserve.

Mr. CAOINETTE: Yes, your money reserve, the cash reserve, it is exact that you have more deposits?

(English)

Mr. PATON: Mr. Chairman, we do not have Mr. MacIntosh with us tonight but we have Mr. Rogers.

Mr. CAOINETTE: We do not need Mr. MacIntosh. You know very well what I am asking and you also know the answer very well.

The CHAIRMAN: Mr. Caouette, I have already ruled that the chief spokesman for the group before us can ask any of his associates or specialists to deal with any question which is put to permit a more informed answer. If Mr. Paton wishes to call on Mr. Rogers, as part of the group testifying before us, rather than answer himself, I have already ruled that is permissible. Also, Mr. Rogers has been waiting patiently in the wings while Mr. MacIntosh has been dealing with some of these very interesting questions and we should give him the opportunity to display the expertise which I am sure he possesses.

Mr. F. L. ROGERS (*Economic Adviser, The Bank of Nova Scotia and Chairman, Canadian Bankers Association Economists Committee*): I think the simple answer here is that Mr. Caouette is confusing inner reserves and cash reserve requirements.

(Translation)

Mr. CAOINETTE: No, what I mean is this, and you have a translation man I hope. What I mean is this: when the Bank of Canada buys a Government security to the amount of one million dollars, this increases by a corresponding amount your cash reserves for the whole chartered bank system. This allows the chartered banks to lend or to increase their lending capacity for  $12\frac{1}{2}$  million dollars for each million dollars in security provided by the Bank of Canada. And this million paid for by the Bank of Canada is added to the actual cash reserve of the chartered banks in this country. Is that true, or not?

(English)

Mr. ROGERS: This has nothing to do with inner reserves, however.

Mr. CAOINETTE: Well it is the reserve, it increases the reserve by that much.

Mr. ROGERS: But this is cash reserve.

Mr. CAOUETTE: It is cash reserve when the Bank of Canada pays cash for an obligation.

The CHAIRMAN: Order.

*(Translation)*

The CHAIRMAN: We are now on the topic of reserves accumulated against losses on loans and investments. It is a restricted field and I think we should clarify the relationships between the topics we are discussing and questions that are put.

Mr. CAOUETTE: Well, Mr. Chairman, there is certainly some relationship between the two. At any time in the year should the Government decide to issue for one billion, or one million, or what have you in securities in the Bank of Canada, with the Government's agreement of course, buys out this security and this increases by the corresponding amount the liquidity, the cash reserves of the Canadian banks. Their reserves do not suffer, on the contrary, the reserve is guaranteed by government action, or by Bank of Canada action. Would it not be claimed that banks are suffering losses, this is not a fact. That is why I want to establish clearly.

The CHAIRMAN: I think we should realize it is quite possible that the witness might be in agreement with you.

Mr. CAOUETTE: The Minister of Finance is in agreement with me. I put questions to him ten minutes ago in the House.

The CHAIRMAN: He is not with us tonight.

Mr. CAOUETTE: He will be with us in a few days.

*(English)*

The CHAIRMAN: Mr. Rogers, have you any further comments to make on Mr. Caouette's question?

Mr. ROGERS: Well, the only thing I could say on the general question of the cash reserves that he is talking about is that the Bank of Canada is concerned about general credit conditions in the country.

The CHAIRMAN: Mr. Rogers, what I am driving at particularly is can you assist the committee by answering Mr. Caouette's question, which is based on the assumption that what he is talking about has something to do with the contingency reserve. Do you have any further comment on that?

Mr. ROGERS: It has nothing to do with that. I can see no connection whatsoever.

The CHAIRMAN: Do you not accept his point?

Mr. ROGERS: No.

*(Translation)*

The CHAIRMAN: Have you any more questions to put at this point.

Mr. CAOUETTE: Mr. Chairman, and I am coming back again to this point. We have had it all well explained in the report of the Canadian Bankers' Association



that the law clearly establishes that every purchase by the Bank of Canada of Canada Government Bonds increases the liquid reserves, I mention the liquid reserves of the bank or chartered banks as a whole. That does not mean that the Canadian Imperial Bank of Commerce, or the Toronto-Dominion Bank loan profit, but all the banks' profits from this, so as to increase the liquid reserves. The witness is certainly not truthful—the reserves are based only on the reserves that come from the deposits of customers, that is not true. The law is the law.

(English)

Mr. PATON: Mr. Caouette, I would like to come to Mr. Rogers support. Perhaps the problem here is that we are using the word "reserves" to describe two entirely different things. If we translated the words "contingency reserves" into "contingency appropriations" it might solve the problem. Appropriations are amounts that by law we deduct from our assets to give a true realizable value of these assets, and the amount that we deduct from these assets shown in our statement here, is the amount that represents our contingency appropriations, if you like. It has nothing whatsoever to do with the 8 per cent cash reserve about which we have had one or two short debates in the last couple of weeks.

Mr. ROGERS: Mr. Paton, if, on the other hand, you talked about cash holdings instead of cash reserves that might help.

Mr. CAQUETTE: I do not care whether you use the word "appropriation" instead of "reserve", or "cash reserve" or another kind of reserve, but the law stipulates that whenever the Bank of Canada buys an obligation from the federal government or any government, then the chartered banks of our country have a supplementary cash reserve added to their normal deposits which constitutes 8 per cent to the Bank of Canada and it gives you the right to multiply it by 12.5 times—this is not new credit but it is an expansion of credit.

The CHAIRMAN: Let me interrupt you. Do you agree with this general proposition?

Mr. ROGERS: No, I do not. This is not the way the system works, and I hope Mr. MacIntosh explained it adequately.

The CHAIRMAN: I am sure he did.

Mr. CAQUETTE: No, it was not explained.

The CHAIRMAN: I would like to try and clear this up. Are these contingency reserves or inner reserves—call them what you like—considered liquid reserves?

Mr. ROGERS: No.

Mr. CAQUETTE: Well, how is that? It is stipulated in the law. It is in the Canada Year Book.

Mr. COLEMAN: Perhaps we should say, Mr. Caouette, instead of talking about reserves, that these are amounts set aside for possible losses.

Mr. CAQUETTE: They do not say that. They say a reserve in addition to their reserves.

Mr. COLEMAN: Inner reserves are amounts set aside for possible losses and they have nothing to do with cash reserves.

Mr. CAOINETTE: So you would have permission to lose 12.5 times what you have as a reserve?

Mr. ROGERS: No.

Mr. COLEMAN: No.

*(Translation)*

The CHAIRMAN: Are there any supplementary questions. Does Mr. Latulippe want to put a supplementary question?

Mr. LATULIPPE: I would like to know, how many kinds of reserves have you?

*(English)*

Mr. ROGERS: Mr. Chairman, it might be of help to note that the section which has to do with appropriations for losses does not use the word "reserves" at all.

The CHAIRMAN: This is the popular nomenclature.

Mr. ROGERS: That is right.

Mr. PATON: It is not too popular.

*(Translation)*

The CHAIRMAN: Do you want to put your question again?

Mr. LATULIPPE: How many kinds of reserves do the banks have? How many have they available to them? Are there several types of reserves, do you have several reserves, or only two or three?

*(English)*

Mr. PATON: Would you like me to answer this? The reserves the chartered banks have which are not disclosed in the statement, Mr. Latulippe, are two in number. One is a tax paid reserve. That is a reserve that is not disclosed but on which taxes have been paid. The second reserve is the general contingency reserve which covers appropriations for contingent situations that might arise with respect to our assets, namely, loans and investments in securities.

*(Translation)*

Mr. LATULIPPE: Are your reserves for bad losses more than adequate?

*(English)*

Mr. PATON: No, sir. They are adequate in the judgment of the Inspector General and the minister in the laid down formula they give us. They are not providing for the present day position but for future contingencies, which we well know will arise.

*(Translation)*

Mr. LATULIPPE: Thank you, Mr. Chairman. That is all for the moment.

*(English)*

Mr. LIND: To get this reserve situation straightened out, you have two types; you have a specific or an inner reserve and a contingency reserve, is that right?

Mr. PATON: As I said to Mr. Latulippe, I was combining them into two reserves. We have a tax paid reserve.

Mr. LIND: Which is it?

Mr. PATON: That is—

The CHAIRMAN: That is not made known to the public.

Mr. PATON: That is not made known to the public.

Mr. CAQUETTE: What do you call that reserve?

Mr. PATON: I am staying with the nomenclature that we have been using.

Mr. CAQUETTE: You have three.

Mr. LIND: Have you three reserves or just two?

Mr. PATON: Let me put it this way. We have (a), a tax paid reserve and (b), we have taxable reserves, that is reserves which are not taxed, and that total is divided into two areas; one, a specific reserve against known situations we have to reserve for and, two, the remainder is a contingency reserve for situations that may well occur in the future.

Mr. LIND: Now, let us go to the tax paid reserve. Is there a formula for setting that out?

Mr. PATON: No, sir.

Mr. LIND: That is, your surplus goes into the tax paid reserve, is that it?

Mr. PATON: The sources of the tax paid reserve will vary among the banks generally, Mr. Lind. There are certain areas in which—

Mr. LIND: I realize that. You are pretty consistent; it is the same type of bookkeeping. Now, in this contingency reserve, which is divided in two, you have a specific reserve and a contingency reserve. This is pre-tax reserve, is it not?

Mr. PATON: Yes, sir.

Mr. LIND: Now, how do you come to the formula? What percentage are you allowed to put into the specific reserve and what percentage are you allowed to put into the contingency reserve?

Mr. PATON: Would you like Mr. Elderkin to respond to that? Perhaps he could give you a more accurate description of how it comes about.

Mr. ELDERKIN: The total amount which may go into the contingency reserve is set by the rules of the Minister of Finance as a percentage and is spelled out to you, Mr. Lind, on exhibit number 14, which has been tabled. Out of that limited reserve, if you will, the specific reserves are allotted. But, the total of the reserves, contingency plus specific, is spelled out and limited by the rules of the Minister of Finance.

Mr. LIND: According to the Porter Commission it is 5 per cent, is that right?

Mr. ELDERKIN: No, that is not. The Porter Commission did not say 5 per cent on the banks.

Mr. LIND: It said 24 times a 25 year loss.



Mr. ELDERKIN: That is different.

Mr. LIND: Which is 4.944.

Mr. ELDERKIN: About five years ago, but not now.

Mr. LIND: It has changed since then?

Mr. ELDERKIN: It changes every year. In the 1965 rules it was 3.48 per cent.

Mr. LIND: 3.48 per cent?

Mr. ELDERKIN: Yes.

Mr. LIND: Now, we have the specific reserve and the contingency reserve, and 3.48 is the figure that goes into the pre-tax reserves? Is that right?

Mr. PATON: That is the peak figure that can be put in.

Mr. LIND: That is the peak figure.

Mr. ELDERKIN: You might also, Mr. Lind, if I may interject, look in exhibit number 14 at the note at the foot thereof where it says the bank had approximately 75 per cent of that maximum.

Mr. LIND: I am going on what they tell me it can go into. I would like to discuss your loss ratio. It states in here

The loss experience of the Canadian banks is naturally relevant in determining the maximum permitted ratio of reserves. In the favourable years since 1950, bank losses on loans have averaged about 1/8 of 1 per cent with the peak year being under 1/3 of 1 per cent.

Is that still substantially true?

Mr. ELDERKIN: That is filed in Exhibit number 12, Mr. Lind.

Mr. LIND: I am taking this from the Porter Commission Report.

Mr. ELDERKIN: Yes, but that Porter Commission Report is a little bit out of date now.

Mr. LIND: Now, why cannot the Canadian banks have the same system as the English banks where they tax these contingency reserves? It would mean more income for the federal treasury, would it not? I will read it to you:

Those opposed to untaxed contingency reserves point to the English banks (which must pay taxes on their general reserves)—

The CHAIRMAN: What page is that, Mr. Lind?

Mr. LIND: That is at page 387 in the left hand column.

Mr. PATON: Would you repeat that? Are you waiting for an answer, Mr. Lind?

Mr. LIND: Yes I was asking why we keep the practice here. Maybe Mr. Elderkin can tell me. Why do we not follow the same practice as the English banks? There must be some reason.

Mr. ELDERKIN: Are you addressing the question to me, Mr. Lind?

The CHAIRMAN: For a start. It may give Mr. Paton and company a chance to ponder your question.

Mr. ELDERKIN: Under the rules of the Minister of Finance there is a general contingency reserve permitted on a percentage basis. Specific reserves are allocated out of that. Under the British system, as we understand it, specific but no general reserves are allowed. This comes back to the administration of the specific reserves and to what extent they are allowed. I am not in any position to comment on how liberal the income tax department of the British government is in allowing specific reserves. It may be that they are very much more liberal than we are here, but that is something we just do not have the information on to decide. If you want to compare this with another authority, in the United States they allow a general contingency reserve in addition to specific reserves.

The CHAIRMAN: Do you gentlemen have something to say at this point?

Mr. PATON: No. I thank Mr. Elderkin for handling the question so efficiently.

Mr. LIND: If you go into the mortgage business you do not need as high a contingency reserve, do you?

Mr. PATON: Our mortgage assets, Mr. Lind, I would assume would come under the eligible assets against which appropriations can be provided.

Mr. LIND: But it would be less than you are operating under now, would it not? The experience of trust and loan companies has been very favourable, has it not?

Mr. PATON: I think our earlier comments this evening indicated that the trust companies had a reserve of 3 per cent, so this is not very far removed from the figure we just received with respect to our contingency reserves.

Mr. LIND: Well, the Porter Commission puts it at 2.8 per cent.

The CHAIRMAN: Do you have any further questions?

Mr. LIND: Yes, I have some further questions. I am just taking a little time to sort them out. I want to go on with the reserves.

Mr. GILBERT: Mr. Chairman, I wonder if Mr. Lind would yield to a supplementary.

Mr. LIND: Certainly.

Mr. GILBERT: Mr. Elderkin, are the specific reserves sufficient without the necessity of contingent reserves?

Mr. ELDERKIN: Well, specific reserves are set up presumably to establish the market value or the realizable value at the time they are established. If you look at the requirements of the balance sheets of the banks, they have to state certain securities other than those of Canada and the provinces at not more than market value. They must set up specific reserves at least to write their securities to market value. They must state their loans after estimated loss thereon. So again they must set up specific reserves at least to cover that. The contingency reserves are not meant to meet the present situation, Mr. Gilbert, as much as to meet the possible loss which cannot be foreseen at that time.

Mr. GILBERT: Thank you, Mr. Chairman.

The CHAIRMAN: Mr. Lind, have you concluded your questions or do you have some others?

Mr. LIND: Yes. There is a statement at the bottom of page 388 in the right hand column—and I would like to direct the question to Mr. Coleman, if I may, Mr. Chairman—which reads:

...the shareholders are entitled to know how their company and its management are performing and, finally, that the discipline of public disclosure is good for management.

What would be your comment on that?

Mr. COLEMAN: Well, those are the views, apparently, of the Porter Report. I think the bankers have different views. We prefer, as Mr. Paton has said I think very ably, to carry on in the present system which has worked so well, and we think that when you talk about losses of only 1/3 of 1 per cent it sounds pretty small, but that is millions and millions of dollars. As the brief says, if any bank suffered a loss of, say, close to 1 per cent it would wipe out the entire year's earnings of that bank.

Mr. LIND: Maybe the amount would not show that year, though.

Mr. COLEMAN: We are speaking of big figures.

Mr. LIND: I realize that.

Mr. COLEMAN: Yes.

Mr. LIND: But do you not think for the good of the shareholders and everything that the banks could modify their procedure here?

Mr. COLEMAN: They could but we do not think it is necessary. As has been said, all information is given to the minister through the Inspector General of Banks. They take a very close look at the appropriations we set up and in their judgment determine if it is right, and I think that the interest of the shareholders and the public are better protected this way than they would be if there was full disclosure.

Mr. LIND: Well, I will take you one step further then. At the top of page 389 it says:

Good accounting practice calls for the disclosure of tax-paid reserves on balance sheets and there is no reason why banks or other financial institutions should be treated differently.

What is your comment on that?

Mr. COLEMAN: Well, I just do not agree with it for the reason I have just given.

Mr. LIND: If as a bank you were loaning money to a company, would you want to know all these facts?

Mr. COLEMAN: I do not quite understand you.

Mr. LIND: Suppose your bank was loaning a substantial amount of money, say \$5 million, to a company, would you want to know about all these inner reserves and everything?

Mr. COLEMAN: I would certainly want to know as much as I could learn, yes.

Mr. LIND: Do you not think the public are entitled to know this about the banks, too?



Mr. COLEMAN: The difference, I think, here is that the Minister of Finance has this information—this point has been argued many, many times—and up to now it has been felt that the system we are working under is the best system in the interests of all concerned. You are suggesting it is a little different with a company and if the officers do not disclose it to anyone, no one would be watching this company except perhaps their own auditors? Is this what you are suggesting?

Mr. LIND: When you say it is the best system, do you consider the system is so good that it cannot be improved upon?

Mr. COLEMAN: I would say any system can be improved upon but I think we have tried to make the point that we think this system has worked very well for many, many years.

Mr. LIND: Well then, could I ask the same question of Mr. Elderkin. Does good accounting practice call for the disclosure of tax-paid reserves on the balance sheets?

Mr. ELDERKIN: I think we are getting close to a policy question, actually, Mr. Lind.

Mr. LIND: I am through. Thank you very much, Mr. Chairman.

The CHAIRMAN: You are through for the time being. Would that not be a fair interpretation of your comment?

Mr. LIND: Through for the evening.

Mr. JOHNSTON: I have a question arising out of the discussion that we have had on inner reserves. I asked some questions about this earlier. I do not know whether things are much clearer now after this evening's discussion or not. However, I am a bit concerned about what it does to the statements and brief comments on the profitability of the Canadian banking industry. I understand that the bank has various reserves and that these reserves earn income, but that not all the income is then reported and so not all of the bank's income will be involved in the .45 per cent of net profit after taxes, and so on, on this sheet.

Mr. PATON: That is correct, Mr. Johnston.

Mr. JOHNSTON: Now, it was suggested earlier that this will balance off with the other companies—

Mr. PATON: Pardon me, Mr. Johnston, perhaps I was a little quick in answering. I heard a voice disagreeing with me when I said, "That is correct". Would you mind making that statement again please?

The CHAIRMAN: Was that voice your conscience or one of your advisers?

Mr. JOHNSTON: I will try again, Mr. Chairman. The proposition I was putting forward, that seemed to follow from the Chairman's questioning of a few minutes ago particularly, was that there were various kinds of reserves and these reserves earned income, not all of which is taxed and not all of which is declared, and not all of which would show in the .45 figure that indicates the net profits after taxes and all other charges as a percentage of total assets?

Mr. PATON: I would like to get this clear before I answer.

Mr. JOHNSTON: Yes.

Mr. PATON: The expression which we have here is "net profits after taxes and all other charges expressed as a percentage of total assets". The "net profits after taxes" figure is the key point. Is that after or before provision for reserves? Mr. Sharwood, do you have the answer to that? With your permission, Mr. Chairman, could Mr. Sharwood come up here?

The CHAIRMAN: Certainly.

Mr. PATON: Incidentally, Mr. Chairman, Mr. Sharwood is the co-author of this very impressive summary.

Mr. G. R. SHARWOOD (*Deputy Chief General Manager, Canadian Imperial Bank of Commerce*): With all due deference to Mr. Paton, Mr. Chairman, I think he gave an incorrect answer to your earlier question. I think disclosure—

The CHAIRMAN: You mean an answer that might have been phrased differently?

Mr. SHARWOOD: That is probably a better way of putting it. I think that disclosure of reserves will have no effect whatsoever on the figures shown here.

The CHAIRMAN: Why not?

Mr. SHARWOOD: Because they are completely unrelated to the figures. A contingency reserve or a specific reserve or any of the so-called inner reserves are not part of either of these equations. It is not part of shareholders capital.

The CHAIRMAN: But if they were listed on the balance sheet where exactly would they go?

Mr. SHARWOOD: Which schedule is it in, Mr. Elderkin? I cannot quite remember. It is schedule "P" where they are shown in next year's annual—

Mr. ELDERKIN: Look at the amendments and not at the bill.

Mr. SHARWOOD: The amendments, yes.

Mr. ELDERKIN: Look at schedule "O" in the amendments. However, on that point, Mr. Sharwood and Mr. Chairman, there is introduced into schedule "O" another factor, in that the appropriations for losses are divided, in effect, between the current year's expenses on a five-year average basis and any remaining amount that happens to be transferred to any reserves.

Mr. SHARWOOD: That is right. I think there are two points here which Mr. Elderkin has brought out, one of which is disclosure. The other is the technique involved in the amendments which have been proposed by Mr. Elderkin and which suggests there is an average of five-year losses. This particular provision will affect the income statement.

The CHAIRMAN: They are reprinted in proceeding number 17 at page 890 and 891, schedule M.

Mr. SHARWOOD: I have them now. You will see the accumulated appropriations for losses, Mr. Chairman, at page 890, item number 9. They are shown above debentures and just after other liabilities on schedule M, which is the annual statement of the bank.

The CHAIRMAN: This is what is published and made available—

Mr. SHARWOOD: To the shareholders.

The CHAIRMAN: —to the shareholders. Where and in which, if any, of these items on the liability side would the concept of either the specific or the contingency reserve be located?

Mr. SHARWOOD: You will see that item 9 is arrived at as the last figure. If you turn to page 892 and look at schedule P you will see that total for the accumulated appropriations at the end of the year, and it will be subdivided into general and tax paid. That will be the total that will be transferred to item number 9 on schedule M.

The CHAIRMAN: These can be made public if these amendments carry? Mr. Johnston?

Mr. JOHNSTON: Well, I am waiting for my answer.

Mr. PATON: I think perhaps we might have Mr. Sharwood clarify the initial answer to the question without getting into schedules O and P, which I do not think was the basic question you asked. You inquired whether this .45 per cent, which was expressed as a percentage of total assets, was the actual gross earnings of the banks.

Mr. JOHNSTON: It was not quite what I was after, I do not think. I was wondering whether there would be a change if you considered the profits you mentioned earlier in your answer to the Chairman's question when you suggested there was a profit unreported because the reserves were undisclosed. I want to know how that would affect this figure or if it would affect this figure?

Mr. SHARWOOD: As I said, Mr. Johnston, I think it is not true to say that this will have very much effect on the reported profit. If you have schedule O in front of you and you look under the expense item you will see, "Other operating expenses including provision for losses on loans based on the five-year average loss experience." Do you see that?

Mr. JOHNSTON: Yes.

Mr. SHARWOOD: Are you following me? Now, that figure has not been previously shown in this particular way, where it is an average of five years, but I do not think it will produce a result materially different from the figures that are shown here. Would you agree with this, Mr. Elderkin?

Mr. ELDERKIN: I think it probably will, Mr. Sharwood, to some extent because we are putting into operating expenses a figure for loss experience, but if you go down to the balance of profits for the year, and take in the appropriations for losses, that will be comparable to the figure you are producing today.

The CHAIRMAN: What will the effect be on the final—

Mr. ELDERKIN: That is comparable to the present published profit after income taxes.

Mr. SHARWOOD: Excuse me, that is the figure that is used in the statement.

Mr. ELDERKIN: That is right. That is the figure that is used in your computations.

Mr. SHARWOOD: I submit that—we have calculated some figures like this—is very similar to the figure I have here.

Mr. ELDERKIN: Oh yes. Well, you go down that far on the schedule.



Mr. SHARWOOD: That is what I intended to do because this is a comparable figure.

Mr. ELDERKIN: Yes, that is right.

The CHAIRMAN: It is very similar.

Mr. SHARWOOD: Yes, very similar. It would be a difference to the second decimal point, .47 or .43, depending—

The CHAIRMAN: Up or down?

Mr. SHARWOOD: It would depend on the particular bank. I have not worked it out for the system.

Mr. JOHNSTON: If I could carry this a bit further. The suggestion, I think, was made earlier that for the trust companies and the sales and finance companies things would balance out in a sense because they have reserves too. But, would they be taxed on all of the profit on their reserves?

Mr. ELDERKIN: Let me interject. If I am correct in this—and I think I am—the trust companies and the loan companies are permitted a statutory contingency reserve of 3 per cent on their mortgages?

Mr. JOHNSTON: Yes.

Mr. ELDERKIN: Before taxes.

Mr. GILBERT: Mr. Chairman, just as a supplementary to attempt clarification, my understanding is that they are only taxed on the income on their reserves, they are not taxed on the reserves themselves.

Mr. ELDERKIN: No. I think probably I was misunderstood. The provision out of profits to create the reserves is considered as tax free. In other words, it is considered as an expense of the year.

Mr. JOHNSTON: There might be something above that.

Mr. ELDERKIN: Well, if there is something above that I presume it is taxable.

Mr. JOHNSTON: I see.

Mr. CAQUETTE: Would they pay taxes on the reserve which is genuinely created by the Bank of Canada?

Mr. ELDERKIN: We are in completely different fields, Mr. Caouette.

Mr. CAQUETTE: You are?

Mr. ELDERKIN: There is no relationship whatsoever.

The CHAIRMAN: Order, please. I do not think Mr. Johnston has finished.

Mr. JOHNSTON: May I ask one more question, then. This is what I have been approaching all along. These figures are fractions of 1 per cent and therefore the differences between them, in a sense, are small. I was wondering if there were complete disclosure and if the proper figure we have been discussing was taken into account and it did alter this .45—there was some disagreement but the suggestion was that it could alter it—the net result of this complete filling in would tend to bring these figures closer together?

Mr. ELDERKIN: If you adopt all of these schedules you will get the complete profit for the year after losses between schedules O and P.

Mr. JOHNSTON: I would like to have your opinion on this. Having done that, and in preparing this same type of statement, would these figures be closer together or the same? Well, they would not be quite the same in percentages because it has already been suggested they would be different percentages. Taking the chartered banks and the trust companies for example, would it be somewhere in between, .55 to .77, or something like that? Would the difference be narrowed?

Mr. SHARWOOD: I think I mentioned already, Mr. Johnston, that we have run some figures on this and the change is in the second decimal place. In other words, it would be .4 something or other. You asked me, "Up or down?" and I said I could not say definitely for the system. I did not have the figures in front of me. In any case, it could not be more than .04 upwards or .04 downwards. It is within the .4 range.

The CHAIRMAN: Mr. Johnston, will you permit me to ask a question. If you look at the first page of your very useful paper on this topic, the figures there are aimed at giving net profits as a percentage of total assets and a return on equity for the 1961 fiscal year. If the statements for all the chartered banks were prepared by taking the figures available for 1961, and if they were all brought together and percentages taken, what would the difference if any be between that result and the result shown on this paper?

Mr. SHARWOOD: I think this is what I am saying, that the figures are not materially different from what are shown here if they were prepared on the same basis as is outlined in the proposed amendment set out by Mr. Elderkin. Mr. Mercure has given me some figures here which might be helpful. The figures for profits before taxes and transfers to appropriations for the three different industries in 1961—which would be before making the changes proposed by Mr. Elderkin, before the transfers to appropriations—was .87 of assets for banks, for the trust companies 1.63 and for the loan companies 2 per cent. I thought that might be helpful to you. They are in table 7-5 and table 10-5 in the Porter report.

Mr. JOHNSTON: Just for clarification, Mr. Sharwood, would you describe those again. Could I have the terminology again. We have one set of figures here now that are entitled, "Net profits after taxes and all others." You have now given me another set of figures. Would you mind repeating what they are?

Mr. SHARWOOD: The definition of those figures is profit before taxes and appropriations.

Mr. JOHNSTON: Thank you.

The CHAIRMAN: I wonder if I may make a suggestion to the committee. We have been dealing with a rather complex topic and as these witnesses are going to be back with us after we have heard some other witnesses, we may feel it would be useful to ponder some of the information that has been given to us on this topic today with a view, if necessary, to returning to this subject when they are next before us. If the committee is in agreement with this suggestion—I am not saying this is the end of all consideration of this topic—then we might consider that the themes specifically raised by the brief have been completed for the time being.

Mr. Caouette?

(Translation)

Mr. CAQUETTE: Mr. Chairman, just a minute ago I had not fully completed the question I wanted to put. I would like to establish the facts, and make the facts quite clearly. I am anxious that Mr. Paton and the other members of the Bankers' Association know I am not attempting to nationalize the banks at all, that is not my purpose. But I want the officials of the bank, like the President of the Canadian Bankers' Association to recognize what we learn from the Canada Year Book of 1965, repeating exactly the same thing as it did in 1964. The Canada Year Book has stated since 1954 and I quote:

(English)

"By virtue of the provision of the Bank of Canada Act, which enables the central bank."

(Translation)

Mr. Elderkin knows all about that.

(English)

"To increase or decrease the total amount of cash reserves"—not contingent reserves but cash reserves—"available to the chartered banks as a group, the Bank of Canada is able to determine broadly the over-all level of the total assets and deposit liabilities of the group and hence of the combined total of currency and bank deposits."

(Translation)

Here Mr. Chairman this is Chapter 25 under the heading.

(English)

"Currency Banking and Miscellaneous Commercial Finance: The chief method"—not the method—"by which the Bank of Canada can affect the level of cash reserves"—not contingent reserves not secondary reserves but the cash reserves—"of the chartered banks and through them the total of chartered bank deposits is by purchases and sales of government securities. Payment by the central bank for the securities it purchases in the market adds to the cash reserves of the chartered banks as a group and puts them in a position to expand"—I understand it is not to create but to expend—"their assets and deposit liabilities. Conversely payment to the central bank for securities it sells causes a reduction in reserves of the chartered banks and makes it necessary for them to reduce their assets and deposit liabilities."

(Translation)

Can we have an explanation now as to why we sometimes have credit restrictions; why we sometimes have expansion in credit and restriction in credit according to what is clearly established in the Bank of Canada Act?

(English)

The CHAIRMAN: Would Mr. Rogers or someone else like to comment?

Mr. CAQUETTE: Mr. Rogers?



Mr. ROGERS: Yes, this is how the system is controlled by the Bank of Canada. The only thing I think that might usefully be added to the explanation is that the Bank of Canada is concerned about the whole financial system, not just the banking system.

Mr. CAQUETTE: But the chartered banks as a group. As I said a moment ago, when the Bank of Canada buys federal government securities for \$1 million it constitutes a cash reserve for the chartered banks and gives you permission to multiply by 12.5 up to date. It might be 14 in a few days but up to date it is 12.5.

Mr. ROGERS: The Bank of Canada does this either by buying securities or selling securities for the purpose of trying to affect credit conditions in the country in the way it thinks is best for the country.

Mr. CAQUETTE: Yes, but the chartered banks have the right to do it.

The CHAIRMAN: Order, please. If I could interrupt right here. I am not trying to suggest that the discussion is not important or interesting—

Mr. CAQUETTE: I think it is.

The CHAIRMAN: Well, we agree it is both important and interesting. However, I must say that as yet it has not been related to the topic of disclosure of accumulated appropriations for losses on loans and investments. I would say that what we are trying to direct ourselves to at this stage are the pros and cons of the matter of disclosure of these items which the bankers' association so elegantly refer to as accumulated appropriations. I guess that is alliteration, is it not? That is what they told me in my grade XIII English course. Losses on loans is another alliteration. I did not know Mr. Sharwood had literary pretensions of that degree and that opetry could enter into so mundane a subject as the disclosure of the inner reserves of banks. I compliment you gentlemen on rising to this literary level.

Mr. PATON: We have other things hidden as well as reserves, such as talent.

The CHAIRMAN: In any event, you will see why I have interrupted you gentlemen. I would suggest that on this specific topic, as I have defined it, and I think I have defined it not unfairly, the discussion in question is not strictly relevant. If that is the case, I would suggest that further discussion in the area that I have interrupted will have to be held off until we again return to this subject.

*(Translation)*

Mr. LATULIPPE: I would have another question, that has come to mind following these other questions. I would like to put it if you would allow.

The CHAIRMAN: I would be very happy to entertain it if it is in order.

Mr. LATULIPPE: I thought of the administrative funds of the United States banks, that the Senate inquiry in the United States looked into lately, and if my information is correct, the administrators have, apart from regular salaries, established these funds. Are there administrative funds of this nature in Canada in Canadian Banks?

Mr. LAVOIE: I do not understand your question.

Mr. LATULIPPE: This reminded me of what is called the administration fund in American banks which the investigation carried out by the American Senate

revealed. If my information is exact, the directors divide this sum amongst themselves, and it is apart from their regular salary. Is there such a thing, in Canadian banks?

Mr. LAVOIE: How do you mean, by dividing amongst themselves, what do they divide amongst themselves, that is what I would like to know, before I answer your question?

Mr. LATULIPPE: There must be a surplus somewhere. You must have surpluses, they certainly have them in Canada.

Mr. LAVOIE: I never heard of it.

The CHAIRMAN: Perhaps you can carry out your own investigation after the meeting has adjourned.

Mr. LAVOIE: Thank you for your suggestion.

Mr. LATULIPPE: This is another type of reserve that Americans appear to have. Is there the same thing in Canada?

Mr. LAVOIE: I am sure there is no such thing in Canada.

Mr. LATULIPPE: I would like to put another question. Does the money supply include only the deposits of the chartered banks?

Mr. LAVOIE: The deposits in chartered banks plus cash, plus the Bank of Canada bills.

Mr. LATULIPPE: In this way the Caisse Populaires, Credit Unions, Trust Companies, Insurance Companies and others do not add anything very interesting to the money supply?

Mr. LAVOIE: No, they do not.

Mr. CAOINETTE: A supplementary question, Mr. Lavoie. How is it then that you maintain that the Caisse Populaire is exactly the same thing as the banks?

The CHAIRMAN: I think I foresee a bit of difficulty. Mr. Latulippe wants to weigh the accumulated reserves, and I cannot find your question in order.

*(English)*

There do not appear to be any further questions which are linked strictly with the topic of the making known of the inner reserves.

*(Translation)*

Mr. CAOINETTE: Mr. Chairman, in regard to the bank reserves?

The CHAIRMAN: Accumulated reserves?

Mr. CAOINETTE: The reserves used to expand the credit of reserves. In 1929 when the economic crisis burst upon us, was this used to cover a lack of reserves from chartered banks, or was it the lack of goodwill to prevent this economic great collapse.

The CHAIRMAN: I am sorry, Mr. Caouette, but I can hardly entertain your question because it has nothing to do, it seems to me at any rate, with this topic of divulging of reserves.

Mr. CAOINETTE: Could we not find out what were the reserves in 1929? What were the inner reserves in 1929 and 1939 when the war broke out and we found all the billions we needed to conduct the war?

The CHAIRMAN: Could you give us a rather quick answer, an answer limited to that point to expedite matters.

Mr. LAVOIE: I have not got the figures with me. I will provide Mr. Caouette with that information tomorrow.

(English)

The CHAIRMAN: We seem to have completed this topic and this means we have completed our questioning at this stage of the specific issues—

Some hon. MEMBERS: Agreed.

The CHAIRMAN: —in the brief, and it was the committee's feeling that the remaining time available today would be for some general discussion. The understanding was that after we heard certain other witnesses, the association would be called back before us to deal with such points as we thought should be dealt with after hearing these other individuals.

Now, out of courtesy to our colleague, Mr. Lambert, who as you know has not been able to remain, I should invite one of the group of witnesses for the bankers' association to make some brief comment on a topic requested by Mr. Lambert, namely, the implications in the banking industry of the computerization of business techniques, and so on. Perhaps he may have some brief comments which can be placed on the record and which may be of interest to the committee.

Mr. PATON: Mr. Power, would you please come to the table? Mr. Power is general manager of administration of the Bank of Montreal.

The CHAIRMAN: I do not know if Mr. Power was watching the clock, or what his feelings were as it moved toward ten, but in any event perhaps we could have him give us some information on this topic, as requested by Mr. Lambert.

Mr. B. W. POWER (*General Manager, Administration, Bank of Montreal*): I will try, Mr. Chairman. Do you want me to just start talking or does somebody want to ask a question?

The CHAIRMAN: Well, if you put it that way you will not be much different from most of the rest of us. To assist you, I think, what Mr. Lambert had in mind was some general comments on the trend of the use of computer technology in the banking industry and the implications for the future of the industry as we know it.

Mr. POWER: Automation in banks in Canada actually followed automation of banks in the United States and there, as here, the problem was the concern over the growing mass of paper to be handled manually by staffs, creating many problems in finding adequate staff, suitable staff, and suitable and adequate space. The banks in the United States became very concerned with this problem in the early 1950's and they devised a system, in co-operation with the computer manufacturers, by which computers could be used to process documents—from the clearing point of view but primarily from a ledger keeping point of view—rapidly and with less staff requirements.



This eventually came to Canada. Canada did not provide a large enough market to develop a system which was distinct from the American system and it had to be similar to the American system. So, in the early development of automation here attention was concentrated on document handling rather than the more advanced uses to which computers are put in manufacturing and other industries. To a great extent this document handling procedure has now been implemented in Canada.

It can go farther if economics permit it do so. In the future we will be going to more advanced uses of computers. These will involve such things as systems of making payments between customers and between banks without the necessity of a written document such as a cheque. I believe that in the fullness of time we will, in fact, have what is referred to as a cheque-less society operating in Canada. I think this will take a long time before it will be in effect but I am sure it will come. This is the type of thing we can look forward to in the future. We can look forward to automated savings, as it is called. It is a system of handling savings accounts in the same way we handle demand deposit accounting now, the posting being done by a computer. The customer will not necessarily be required to appear at his home branch in order to cash a cheque or make a transaction. All branches in an area, as we picture it, will be connected with a simple computer which will handle all the account keeping for savings accounts at one location. Passbooks, if they are continued in use, will be posted automatically at the tellers wicket by a computer in a remote location.

These are the types of things that are going to come. They are going to be developments which will enable bank management to manage better through better management information. This type of thing is being developed by banks now in the United States and here. This is just a general picture.

I think some of the members of the committee are interested in whether or not these developments, and others connected with electronics, will result in a diminution in the number of branches. I think not. I cannot see any reason why that should happen. An American consultant has recently predicted that it will happen. I never heard of this consultant before and I never heard any other American consultant or banker make such a prediction. I think what will happen is that it is quite possible we will have more branches and will be able to serve the public better, because many of the people now or in the past who have been engaged in routine work of an uninteresting nature which really was rather non-productive will be relieved of that work by the computer and made available to serve the public better.

The CHAIRMAN: You are not referring to general managers?

Mr. POWER: I could be.

Mr. CAQUETTE: Are we going to have automatic managers so that the credit will be easier than it is sometimes?

Mr. POWER: There are credit scoring systems being developed, Mr. Caquette, that may, in fact, make the job of granting credit much easier than it is now.

The CHAIRMAN: This is all being recorded, you know. Does the committee have some brief questions of our witness on this very interesting subject? We are getting very close to ten.

Mr. LIND: I just have one question. Is this the best system, Mr. Power?

Mr. POWER: As a practical matter for Canadian banks it is the best system. There might be better systems developed but until they are developed and put into use in larger markets than the Canadian market they will not be available to us. This equipment is terribly expensive to develop and only the United States is large enough, through eventual sale of computer units, to provide the funds for development.

Mr. LIND: May I ask one further question. Will these computer systems be developed by each individual bank?

Mr. POWER: The detail of the system design is done by each individual bank but there is not too much room for variation. There is a great similarity among them all.

Mr. LIND: This is not what I mean. Will this be pooled for all the banks or will each bank have their own computer system?

Mr. POWER: Well, up to now each bank has its own computer system. We in the Bank of Montreal have installations in Montreal, Toronto and Vancouver. Some of the other banks are located with their own systems in some or all of these places. We are looking at the possibility of joint operations in smaller places which now are not large enough to warrant a computer for any one bank. However, we are not ready for that yet.

The CHAIRMAN: Any further brief questions of Mr. Power?

Mr. LIND: I have just one final question. Once you get the banks working together like this on one computer system will this eliminate competition?

Mr. POWER: Not at all. The time has long since passed when being first to install a computer was a matter of competition. There is no prestige involved now.

Mr. LIND: I do not think that is exactly what I meant.

Mr. CAOINETTE: After Toronto, Montreal and Vancouver, do you think that it would be appropriate to install a computer system up in Rouyn-Noranda?

The CHAIRMAN: Are you planning to put one in your dealership?

Thank you, Mr. Power. Now, our next meeting will be Tuesday at 11 o'clock. Our witness at that time will be Mr. Douglas Gibson, former executive vice-president of the Bank of Nova Scotia and I believe also a member of the Porter Commission. I also understand that some of our witnesses we have had with us for the last several days will be remaining and they will be available to follow our proceedings and deal with such matters as may arise. I think we can excuse them for the time being. Do you have any parting words which will not bring about undue controversy?

Mr. PATON: Should I say that parting is such sweet sorrow? I would like to say on behalf of myself, Mr. Lavoie, Mr. Coleman, Mr. Hackett, Mr. MacIntosh, Mr. Rogers and Mr. Power and the Association as a group that we have been very much impressed with the co-operation and kindly manner in which the

committee has received us. They have put their questions to us fairly and listened quite patiently notwithstanding that we probably misunderstood them now and again.

We have been very much impressed and we appreciate the courtesy you have shown us. We certainly will be on deck here when needed on Tuesday and whatever following program is necessary. Thank you, Mr. Chairman.

The CHAIRMAN: This meeting is adjourned until next Tuesday.



















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OF  
PROCEEDINGS AND EVIDENCE

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LÉON-J. RAYMOND,  
*The Clerk of the House.*

HOUSE OF COMMONS

First Session—Twenty-seventh Parliament  
1966

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STANDING COMMITTEE

ON

**FINANCE, TRADE AND ECONOMIC AFFAIRS**

*Chairman:* Mr. HERB GRAY

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MINUTES OF PROCEEDINGS AND EVIDENCE  
No. 27

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TUESDAY, NOVEMBER 29, 1966

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Respecting

Bill C-190, An Act to amend the Bank of Canada Act.  
Bill C-222, An Act respecting Banks and Banking.  
Bill C-223, An Act respecting Savings Banks in the Province of Quebec.

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WITNESS:

J. Douglas Gibson, former Executive Vice-President, Bank of Nova Scotia,  
and former member of the Royal Commission on Banking and Finance.

ROGER DUHAMEL, F.R.S.C.  
QUEEN'S PRINTER AND CONTROLLER OF STATIONERY  
OTTAWA, 1966

STANDING COMMITTEE  
ON  
FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. Herb Gray

*Vice-Chairman:* Mr. Ovide Laflamme

and Messrs.

Addison,	Comtois,	Latulippe,
Basford,	Flemming,	Lind,
Cameron ( <i>Nanaimo-</i>	Fulton,	McLean ( <i>Charlotte</i> ),
<i>Cowichan-The Islands</i> ),	Gilbert,	Monteith,
Cashin,	Irvine,	More ( <i>Regina City</i> ),
Chrétien,	Johnston,	Munro,
Clermont,	Lambert,	Valade,
Coates,	Lamontagne,	Wahn—(25).

Dorothy F. Ballantine,  
*Clerk of the Committee.*



## MINUTES OF PROCEEDINGS

TUESDAY, November 29, 1966.  
(52)

The Standing Committee on Finance, Trade and Economic Affairs met at 11:10 a.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Addison, Cameron (*Nanaimo-Cowichan-The Islands*), Chrétien, Clermont, Flemming, Gilbert, Gray, Irvine, Laflamme, Lambert, Latulippe, Leboe, Monteith (13).

*Also present:* Mr. Johnston.

*In attendance:* Messrs. J. Douglas Gibson, former Executive Vice President, Bank of Nova Scotia, and former member of the Royal Commission on Banking and Finance; C. F. Elderkin, Inspector General of Banks; Miss M. R. Prentis, research assistant.

The Committee resumed consideration of the banking legislation and the Chairman introduced the witness, Mr. Gibson.

At the request of the Chairman, the witness summarized his brief, copies of which had previously been distributed to the members. In accordance with the resolution passed at the meeting of October 13, 1966, the brief is attached as *Appendix R*.

The witness was questioned, and at 12:55 p.m. the Committee adjourned until 3:45 p.m. this day.

### AFTERNOON SITTING (53)

The Committee resumed at 3:55 p.m. this day, the Vice-Chairman, Mr. Laflamme, presiding.

*Members present:* Messrs. Addison, Cameron (*Nanaimo-Cowichan-The Islands*), Clermont, Flemming, Gilbert, Laflamme, Lambert, Latulippe, Leboe, Lind, Monteith (11).

*Also present:* Mr. Johnston.

*In attendance:* The same as at the morning sitting and Mr. Denis Baribeau, research assistant.

Questioning of the witness was continued and at 6:00 p.m. the Committee adjourned until 8:00 p.m. this day.

## EVENING SITTING

(54)

The Committee resumed at 8:15 p.m., the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Cameron (*Nanaimo-Cowichan-The Islands*), Clermont, Comtois, Flemming, Gilbert, Gray, Laflamme, Lambert, Leboe, Lind, Monteith (11).

*Also present:* Messrs. Grégoire and Saltsman.

*In attendance:* The same as at the afternoon sitting.

The Committee resumed questioning of the witness.

At 9:05 p.m. the Vice-Chairman, Mr. Laflamme, took the Chair at the request of the Chairman.

Questioning of the witness being concluded, the Vice-Chairman thanked him for his contribution to the deliberations of the Committee. The witness, in turn, thanked the Committee for their reception of his brief.

At 9:45 p.m. the Committee adjourned until 11:00 a.m., Thursday, December 1, 1966.

Dorothy F. Ballantine,  
*Clerk of the Committee.*

## EVIDENCE

*(Recorded by Electronic Apparatus)*

TUESDAY, November 29, 1966.

The CHAIRMAN: Gentlemen, I see a quorum. Our witness today is Mr. J. Douglas Gibson, and I think he is a well known personality in the business community of Canada. He is a former executive vice-president of the Bank of Nova Scotia, and a former member of the Porter Commission.

We are pleased to have you with us this morning, Mr. Gibson, and I invite you to present your brief to us in summary form.

Mr. J. Douglas GIBSON: Thank you very much, Mr. Chairman. I appreciate the opportunity of appearing before this Committee, and I will try to make my remarks as an addition to my brief, as short as possible. I should emphasize that I am speaking as an individual. I am not speaking on behalf of the banks, and, needless to say, I am not speaking on behalf of the Royal Commission on Banking and Finance, of which I was a member, although I am in full agreement with the conclusions of that commission.

I think perhaps it would be best, if I ran over some of the principal points that strike me as being important. I think it is a very encouraging thing to see the emphasis on the competitive philosophy that appears in this Bill No. C-222, in the form of lessening of restrictions on the banks. In my view, and I think there is a great deal of evidence to support this, competition is the best assurance of efficiency in the kind of economic society that we are living in at present. We are living in a very highly competitive world, and we as a country have been moving toward a more open kind of economy. It seems pretty evident that if we are going to keep up in the kind of rapidly changing world that we are living in, that this is the right course to follow to keep ourselves open to competition, to try and keep up in this competitive type of world.

As a country, we have tended to promote economic efficiency, and higher living standards, through open competition rather than through protective policies. I say that this has been the tendency in the last 25 or 30 years. It is pretty clear, I think, that the restrictions on the chartered banks have had the effect of protecting certain other financial institutions in our society; and what is more important, they have had the effect of denying access to cheaper forms of credit to certain members of the community, particularly smaller business people, smaller borrowers. The 6 per cent ceiling as I emphasize in my brief, has been the most important restriction. Although the restrictions resulting from the requirement to keep cash reserves higher than were needed, and particularly to keep out of the high cash reserves against term deposits, worked against the banks competing as effectively as they might, since their competitors were not subject to the same restrictions.



The other restriction, which the bill proposes to remove, gradually, is the restriction on taking mortgage security and making mortgage loans. In my comments in the brief I make the point that the removal of these restrictions should be helpful. I would like to say something else about this from another point of view. The chartered banks are the only organization in Canada which has a nation-wide system of branches, and a group of people in those branches who are trained to lend money. They are not all of equal quality, but by and large they are a pretty good group of people. This system goes right across the country, and I think there are 6,000 or 7,000 branches. In addition to having the physical facilities and staff, who know about lending money, the chartered banks have connections to do business with most of the businesses in this country; practically all of them have an account with one chartered bank or another. They are the only group of institutions that have connections with all the small businesses in the country, in effect, and all the medium sized businesses.

What I am saying is simply this: we have these facilities; they are being used to a degree, but they are not being used as much as they might be. They are not being used, in particular, for providing medium term loans, or longer term loans, to small and medium sized businesses, to any very great degree. There are quite a few reasons for this. I think one should recognize, right at the beginning, that with money as tight as it is, it would be very difficult for the chartered banks to substantially expand their loans of this character and in this direction. But my understanding of the Bank Act revision is that what you are trying to do is to plan a proper framework looking 10 years ahead, not just in terms of the current, rather unusual, situation where money is extremely tight. The fact is that the present law, 6 per cent ceiling, the cash reserve requirements, and the mortgage restrictions, make it virtually impracticable for the chartered banks to expand in the direction of more term loans to small and medium sized businesses.

As I say, they are the people who have the facilities; nobody else has these facilities across the country. The banks have been increasingly becoming the principal people providing funds to smaller businesses. The money market does not provide funds to smaller businesses; a lot of the other institutions are not organized to do this sort of thing. It seems to me that it is very important from a national point of view, thinking in terms of the effective use of our resources, that we use these facilities and use them effectively. I think this is the strongest argument for taking off restrictions.

We do have other facilities in this area, of course. The Industrial Development Bank, for example, has a certain number of offices; but they are not subject to the restrictions, which I have mentioned, that the chartered banks are. In fact the Industrial Development Bank makes loans at substantially higher rates than the chartered banks' ceiling. Unless we are thinking in terms of expanding facilities in other directions, on the part of government, or on the part of near banks, and if we are really concerned about getting as much money available, as economically as possible, to small and medium sized business, it seems to me very important that these restrictions be taken off the chartered banks.

Incidentally, I would like to just note that the Royal Commission on Banking and Finance recommended that the 6 per cent ceiling on bank interest

rates be removed regardless of other changes that the government might propose to make in the Bank Act.

Now, one thing that I tried to bring out in my brief was the question of how the banks would react to a removal and an easing of restrictions. I do not think that one should look at the banks and say, "well, are these people going to do the right thing or the wrong thing; are they good fellows or are they not such good fellows". The right way to look at this, once we have a competitive type of economy with a profit and loss system, is to say, "are the incentives of a kind that will persuade them to do the things that are needed in the economy?". It seems to me this is really the question, to get the incentives so that the banks can be expected, in their own interests, to push in the directions that are desirable from a national point of view. I think there are some exceptions to this broad and competitive approach in the bill which you are studying.

I would like to say a very brief word about Clause 76, which I regard in part as an exception to the idea of a wholly competitive approach. Clause 76 you will remember is the clause which proposes to limit bank ownership in any other type of company, whether financial or otherwise actually, to 10 per cent of the voting common stock. It also proposes, and this is the feature that I want to speak about, to make retroactive the application of this 10 per cent rule to arrangements that have been made between banks and other financial institutions in recent years, indeed going back as far as you like. It seems to me there are two objections to this business of asking banks to undo what already has been done. One is, the retroactive feature; in my view, one does not make something retroactive unless there is a very good reason for it. One does not ask people to undo contracts and arrangements that have been made, and grown into place, and so on, without having a good reason. There may be good reasons in this case, but I have not heard them stated.

I would like to quote very briefly from what the report of the Royal Commission on Banking and Finance said on this subject. The Royal Commission went farther than this bill; they did not want them to acquire any shares in other financial institutions; they wanted to limit them to 10 per cent of other deposit taking institutions, and they wanted to limit them to 10 per cent of holdings in other financial institutions. The Royal Commission did not automatically say that what was done in the past should be undone again. They expressed the view, and this is on page 372 of the Royal Commission's report, that the Treasury Board—whom the Royal Commission suggested should be the final authority to decide whether or not previous arrangements should be changed—they expressed the view that the Treasury Board should be empowered to inquire into transactions involving banking institutions, and this includes trust companies, and I quote:

—which have occurred in recent years and which would have required approval under the rules suggested above.

They go on to say:

In cases where the authorities find that the public interest is in jeopardy, they should have the power to apply effective remedies.

Now, if you read this commission's report, the public interest in preventing concentration was mainly defined as preventing any actions which would reduce

competition, or limit competition. In this context what this statement means is that if it can be shown that the arrangements that had been made are limiting and restricting competition, and therefore are prejudicial to the public interest, and consequently, the public's interest—to use the report's word—is in jeopardy, then there should be power to apply effective remedies. This is quite a different approach from the approach contained in the bill, which simply says that these things should be undone, and that the banks should be given—taking the date here—about 4½ years to undo such arrangements. I suggest that this is a rather unusual approach, and it seems to me that it be desirable to have good reason to do this, as a matter of principle.

Now, the other objection to the approach in clause 76, which I think is very important,—this is in addition to the retroactivity of the section—is that it does seem important that we do not restrict good initiatives in the financial system, good new ideas, good new types of service that might be performed and given to the public. Again, I would like to quote very briefly from the report at page 371 where it says:

—we would not wish to see legislation—

That is the legislation limiting, or preventing, or prohibiting bank purchases of securities in other financial institutions. I continue:

—we would not wish to see the legislation inhibit useful innovations and improvements in the financial system by preventing or unduly restricting the participation of banking institutions in new joint ventures with other businesses or with other members of the financial community. In situations of this kind, of which there have been a few recently,—

And one might refer to RoyNat, or the Mortgage Insurance Company of Canada, as examples.

—Treasury Board approval might be almost automatically forthcoming provided that the institution concerned has less than a controlling interest.

Now, that was one of the commission's suggestions, which is not in line with the bill. The commission kept emphasizing what we are trying to do here is to induce competition; we do not want to permit concentration that will lessen competition, but the idea of inducing, and encouraging competition, is the basic idea. Some of these initiatives that banks have taken have added to financial services, and I think one can say, have induced a wider degree of services, which is certainly desirable.

One other subject, which I said a bit about, and which I think is the most difficult subject, in a lot of ways, facing the Committee, is the question of foreign banking. This is certainly a real problem, and I do not pretend to know the answers to it. I have some views on it. I do not think one can just apply without qualification the principle of competition here. There is a problem of concentration here as well. We say that we do not want to see undue concentration in our own economy. I think we must recognize, if we look at North America, that New York is the centre of a great economic concentration of power, and that the big banks operating out of New York are part of this concentration. Therefore, I do not think you can just say "oh, we should allow open competition here".



Certainly, I would not want to see the great American banks controlling the Canadian banks.

Now, the Royal Commission's approach on this was the foreign bank purchase of shares; in other words, foreign banks purchasing shares in Canadian banks, should not be permitted to do so without applying to the Treasury Board and getting their approval. It goes farther in this respect even than this bill. We say well, look, we do not like the idea of this kind of concentration. It is not just a domestic problem, the problem of concentration; it is an international problem too, and we just do not think that foreign banks should be permitted to purchase shares in Canadian banks without the approval of the Treasury Board, or the Canadian government. This is a more direct approach than the one in the bill, and I prefer it to the one in the bill. I am a bit doubtful, both about clause 53 and clause 75(2) (g). Clause 53 is the clause which limits ownership in a bank, on the part of an individual or a corporation, or an associated group, to 10 per cent of the outstanding shares; and also limits foreign ownership, in whatever form, to 25 per cent of the outstanding shares. Clause 75(2) (g) is the clause which limits the expansion of banks where the ownership is concentrated to a greater degree than the 10 per cent, and this, of course, applies only to the one bank.

An hon. MEMBER: The Mercantile Bank.

Mr. GIBSON: Yes, sir. It limits the expansion in their assets and liabilities to 20 times their authorized capital. The 25 per cent section—a portion of clause 53—and clause 75(2) (g), can be said to be discriminatory, because the 25 per cent applies only to foreigners, and the 75(2) (g) applies to only one bank, which happens to be a foreign controlled bank. I think that there are real objections to discrimination. One is that this kind of discrimination is not in line with the broad trend of Canadian policy, which has been toward a more open type of economy. The other is that if you discriminate, then other countries are apt to take what you do as a reason for discriminating against you. We have heard recently quite a bit about reciprocity in Canada-U.S. banking relations. I do not think the 10 per cent clause in clause 53, is discriminatory because it applies to everybody, Canadians and foreigners, alike. But it does in fact limit a foreign bank, or anybody else, from acquiring more than 10 per cent ownership in a company.

I do not see any real reason for the 25 per cent, provided that you limit the owners to the concentration of ownership abroad; and the 10 per cent does limit the concentration of ownership abroad. There is very little difference in terms of its effects on Canada whether you have a lot of shareholders spread around Canada, or some of them spread around the United States, Britain, and elsewhere. If they are relatively small shareholders, this does not affect the policies of the institution concerned; and in terms of its effect on our society, I find it very difficult to see any difference between the shareholder who lives in Cleveland who has, say, 100 shares of a bank and one who lives in Ottawa, or one who lives in Birmingham, England. It seems to me that there just are not any real effects that flow from this.

What we have to be concerned about here, in my view, is the question of concentration, of control by foreign banking institutions, and the 10 per cent does give some real protection there. In other words, I would say, if it is regarded as necessary to try and prevent foreign institutions from controlling

Canadian banks,—and I think it is—that we need something like this 10 per cent restriction on ownership in any one place—the Royal Commission would go even farther than that—but I do not think we need to do it in a way which is discriminatory, and can be interpreted as discriminatory, in other countries.

The last point I made in my brief was in regard to the supervision of financial institutions. As you know, the Royal Commission's report took a pretty different sort of line from the bill before you in this direction. The Royal Commission suggested that banking be defined, something that never has been done before, at least not within living memory. And that since banking is under the federal government, under the British North America Act, that those institutions that perform banking functions should be subject to this extent at least to federal supervision. Now, the government is not proposing to follow this kind of line. It is not for me to say what the reasons might be, but the approach in the bill to this problem of regulation is in effect through greater federal-provincial co-operation.

I should not say that this is really in the bill; this comes out of what the Minister said about this general area, and through the proposed institution of a deposit insurance scheme. There is no question that greater federal-provincial co-operation is necessary in this whole area. Even if banking were defined as the Royal Commission suggested, it would be very, very necessary to have a high degree of federal-provincial co-operation in this area. If banking is not defined, it is very much more important. The necessity of a high degree of co-operation between provincial and federal authorities becomes very great indeed. Why do you need this high degree of federal-provincial co-operation? One reason is to bring in almost all the deposit taking institutions. You have to bring most of them in—the great, vast majority—if you are going to have effective supervision. In order to do this, you obviously need federal-provincial co-operation. The other reason is, of course, to set adequate standards of supervision.

We have to have some reasonable understanding of what kind of supervision, how far we would go on supervision, under a deposit insurance scheme; otherwise, deposit insurance would not do the job that is envisaged for it. Deposit insurance could be very successful financially; this would not pose very much of a problem, if, as is proposed, the federally incorporated institutions—the chartered banks and the federally incorporated trust companies—were automatically in, and had to pay the premiums. But it would not be successful financially; for a deposits insurance proposal is not the criterion of its success; the criterion of success of a deposit insurance plan in Canada, if we were to put one in, would be whether it brought in almost all of the deposit taking institutions in the country, and whether it set good, and acceptable standards of supervision. I think I have said enough, Mr. Chairman.

The CHAIRMAN: Thank you very much, Mr. Gibson, for your very useful expansion of the remarks in your brief. May I suggest to the Committee, that in line with our experience with our previous witnesses, that we might consider discussing the brief in the order of the topics presented. It seemed to me that the topics were presented in the following order, and I am subject to correction on this: there is a general discussion of the matter of the interest rate, into which Mr. Gibson brought some references to cash reserves and term lending generally,

followed by discussion of the limitation of 10 per cent on the ownership of banks, and other bodies and directorates.

Mr. GIBSON: Reserves first.

The CHAIRMAN: Yes, that is what I said.

Mr. GIBSON: No, reserves.

The CHAIRMAN: Yes, well I said the interest rate, reserves, the 10 per cent limitation, which I suppose would include questions of boards directors and so on; the matter of foreign control of our banking system, and then concluding with deposit insurance. Does the Committee agree that this seems to be the order of their presentation?

Mr. GIBSON: Yes, except, Mr. Chairman, that there is definition of banking before the last one.

The CHAIRMAN: Yes; may I suggest that the definition of banking be considered and discussed, Mr. Gibson, as part of the discussion of deposit insurance?

Mr. GIBSON: It is really part of the control of banks and near banks.

The CHAIRMAN: Yes, but not in the sense of control by government abroad.

Mr. GIBSON: No, supervision.

The CHAIRMAN: Does the Committee agree that this would be an appropriate order to follow?

An hon. MEMBER: Is this right to the end, Mr. Chairman?

The CHAIRMAN: Yes; I am taking the order in which Mr. Gibson seems to have raised the major topics in his brief. First, the broad question of the interest rate, which would bring into account matters of term lending and so on, followed by the question of reserves; then the matter of the 10 per cent limitation of ownership by banks of shares of other firms, and I include in this matters of interlocking directorates and so on; followed by the broad question of control of our banks by foreign interests; and finally the question of government supervision of banks and financial institutions, and deposit insurance. I am outlining this in a broad sense with a view to having an orderly discussion with our distinguished witness. You may recall that we followed this system with some success when we had the bankers' association before us. I invite members of the Committee to signify to me their interest in asking questions. I already have Mr. Monteith, Mr. Lambert, and Mr. Clermont, I see Mr. Cameron, Mr. Leboe, Mr. Laflamme, and Mr. Gilbert.

An hon. MEMBER: Is it expected that Mr. Gibson will be here throughout the day?

The CHAIRMAN: This is our hope, subject to exigencies of House business, and that sort of thing. I believe you are available today, Mr. Gibson?

Mr. GIBSON: Yes, I am at your disposal today.

The CHAIRMAN: I recognize Mr. Monteith now.

Mr. MONTEITH: Mr. Chairman, I wonder if I might ask you a question just for clarification, prior to asking Mr. Gibson any questions. Was it your interpretation yesterday from what the Minister said during our discussion on the



extension of the present bank legislation, that he proposed to bring in the deposit insurance bill and give it first reading? Did that mean before Christmas, or at this session? I have not seen yesterday's *Hansard*, so I do not know exactly what was said, but there was some intimation that he would be giving it only first reading at this stage, and then it would be available. Now, I do not know whether he intends to refer it to this Committee, or what.

The CHAIRMAN: Frankly, I could not answer your precise question.

Mr. CHRÉTIEN: The bill is in the drafting process now, and we think we will be able to have this bill in the House of Commons within a few days, perhaps this week or next week; we do not know because the technical staff is quite busy right now, and that is why we are obliged to wait. But I am quite sure that we will have that at the beginning of next month.

Mr. MONTEITH: There was some statement by the Minister yesterday to the effect that it would be given first reading only; I did not know what he meant by that, that was all. I will just leave it with you, Mr. Chairman.

Mr. CHRÉTIEN: I was not present when he made his statement, but we have to have the bill, and I am quite sure we will receive it very soon.

Mr. MONTEITH: I think it will be before it is in the House. Now, is it going to be referred to this Committee, or are we just going to be aware of it, and go ahead and work on it without reference?

Mr. CHRÉTIEN: Yes, but Mr. Monteith, we are obliged to wait until after second reading for that.

Mr. MONTEITH: This is my ordinary thinking, yes.

The CHAIRMAN: I think that our position would be this: while we could not consider the bill as such, in the sense that we would make recommendations to the house upon it, we certainly would be able to refer to it specifically in the course of our study of the bills that are before us, namely, the Bank Act, the Bank of Canada Act, and the Quebec Savings Banks Act. I certainly intend to permit a very detailed reference to it, in the course of our consideration of the bills which are before us.

Mr. MONTEITH: Well, I will just leave it with you, Mr. Chairman, in this manner: that I would like some clarification of what was meant by the first reading. Now, maybe I can find out myself if I see yesterday's *Hansard*.

The CHAIRMAN: Of course, Mr. Chrétien, the minister's parliamentary secretary, has heard your very useful question, and perhaps he will report either to you directly, or to the full Committee on the government's intentions in this regard.

Mr. MONTEITH: Thank you. Mr. Gibson, there is only one brief summary of questions I would like to ask you concerning interest rates. I think it is safe to say, to all general purposes at least, that the maximum of 6 per cent today has become the minimum; is that assumption right?

Mr. GIBSON: Generally speaking, I would think so.

Mr. MONTEITH: We have been told by the Canadian Bankers' Association that if this bill were to be passed by the end of the year—and undoubtedly it will

not be—that probably the new interest maximum would be  $7\frac{1}{4}$  per cent, or approximately that; is that your guess?

Mr. GIBSON: The formula seems to work out to that; it might be higher, but I think  $7\frac{1}{4}$  is about right.

Mr. MONTEITH: Is there any danger of that maximum becoming a minimum?

Mr. GIBSON: Well, Mr. Monteith, I would doubt it. I am not a practising banker, at the moment, I have been out of banking for a year; but I would think that would give enough room so that there would be a structure of rates. Admittedly, money is very tight at the moment, but I would think there would be a group of rates under that. I think you should ask the bankers about that, though, as well.

Mr. MONTEITH: I was really asking you for your opinion on it.

Mr. GIBSON: Well, that would by my view, that there would be a structure of rates. I do not know what the minimum would be; it might be a shade higher than the present 6 per cent, but I do not think it would be  $7\frac{1}{4}$ .

Mr. MONTEITH: If the formula permitted a further increase as time went on, might the tendency to have a maximum the minimum mean that the minimum, which you say might just reach over the 6 per cent a bit now—there would be a spread in there—would increase if this maximum were to increase?

Mr. GIBSON: I would like to be quite clear on this. I did not say that the minimum would go over 6 per cent; I said it might go a shade over 6 per cent, but I do not really know. This is a matter of judgment. I do not think it would go very much over 6 per cent. There is, of course, a tendency for interest rates to be rising; that is, interest rates are rising by definition. If this maximum rate of  $1\frac{3}{4}$  per cent above the short term interest rate on government of Canada bonds is rising, then interest rates generally will rise. So, I think you would be correct in assuming that the general trend of interest rates was upward at that time. This is the reason, of course, that we are increasing the ceiling, so that you can have a spread under the maximum. All I can say is that I would hope that interest rates are not going to rise much more; it seems to me they are pretty high now. I am not talking about bank interest rates, because they are restricted, but the general interest rate structure is pretty high. We are in a period of really tight money, not just in Canada, but abroad.

Mr. MONTEITH: Could I ask then—and this is purely for an opinion, and the Bankers' Association did give us an opinion on this, a pure guess, mind you, and I am just asking you for a guess—when, under the proposed formula, might the ceiling be removed entirely?

Mr. GIBSON: I could not give you an intelligent opinion on that; I wish I could. I would hope that it would be in the next two or three years, but I just do not know. You have got to make a guess about the whole state of the world's economy when you are answering this question.

Mr. MONTEITH: You do not see it in the immediate future, by any means?

Mr. GIBSON: No, I certainly do not, but I would hope it would happen within a reasonable period of time.

Mr. MONTEITH: In your opinion, would it be wiser to remove the ceiling entirely at this stage, in this legislation, rather than to have this ceiling formula

which is set out? In other words, I have felt in my experience in a lot of phases of life, such as the question period in the House of Commons, that the maximum is inclined to become the minimum.

An hon. MEMBER: And vice versa.

Mr. MONTEITH: But I am just wondering if that tendency could be relieved at all if the ceiling rate was removed entirely at this stage?

Mr. GIBSON: I am not sure, sir, that I could accept the analogy between the question period in the House and the maximum on interest rates, although it is a very interesting one. I would prefer to see the ceiling taken off altogether; I do not think it makes any sense. That is simply my view. I signed this report, and we said the ceiling should be taken off regardless of the other things that the government proposed to do under the Bank Act, and any other legislation concerning financial institutions. I have not changed my view on that.

Mr. MONTEITH: One final question then: if this formula is followed, you are not of the opinion that the maximum will necessarily become the minimum; you are of the opinion that there will be a spread, possibly starting at a minimum of maybe something higher than the 6 per cent, but at the same time that there will be a spread between that minimum and the maximum of something in the neighbourhood of the present rate.

Mr. GIBSON: Yes; I am strongly of the opinion that there would be a significant spread.

Mr. MONTEITH: That is all for now, Mr. Chairman.

The CHAIRMAN: Mr. Lambert, followed by Mr. Clermont.

Mr. LAMBERT: Mr. Gibson, just following on with what you said, though I am not quite as sanguine as you are in this regard, in that the government's recent action in raising the mortgage interest rate under the National Housing Act to  $7\frac{1}{4}$  per cent means that  $7\frac{1}{4}$  per cent would be the ceiling under the proposed formula for the present time. N.H.A. mortgage lending is possibly the safest kind of operation really, since it is insured, and there is the moral responsibility of government behind the loan. When we consider this safest kind of lending with a rate of  $7\frac{1}{4}$  per cent, how can you say that on the other type of equity, or commercial lending, the rate could conceivably be less if the security is not as good; that is, there is a greater risk?

Mr. GIBSON: In the first place, the N.H.A. rate applies to long term money. This is a long term rate; your money is tied up. In the second place, there is quite a lot of work in connection with N.H.A. loans, and there is a spread between N.H.A. interest rates at the present  $7\frac{1}{4}$  per cent, and the short term rate—to take the other extreme of as low a risk as you can get—on government of Canada paper of about  $1\frac{3}{4}$  per cent, or something of this order. Now, I suggest to you sir, that the kind of loans, and investments that the banks are dealing in would fall in the range between short term government paper, N.H.A., and some of them in a free market that go above N.H.A. rates. But a lot would fall in between the present 6 per cent and the present  $7\frac{1}{4}$  per cent rate, which you and Mr. Monteith have indicated.

Mr. LAMBERT: Under the government proposal, of course, it is readily understandable that there are these ranges, or this spectrum for interest rates, as



you indicated, down to the highly competitive rate on government paper. Then you have the ceiling of  $7\frac{1}{4}$ , and then you have the sphere exempt from any interest ceiling, as provided for under clause 91, which, I suggest, will attract a greater and greater retention of the bank's business in the future, if the legislation goes through.

Mr. GIBSON: I think this is true, sir, that as more money becomes less tight the mortgage lending end would tend to increase, whether through the actual purchase of mortgages or through term loans to smaller businesses; it is really a very similar kind of operation.

Mr. LAMBERT: Now, with respect to the proposal of the Porter Commission that the ceiling on interest rates be eliminated, was this only part of the thinking of the commission, and there was to be included, as well, much greater supervision of the monetary or financial institutions of the country? In other words, this is a package deal, and one cannot isolate the two things: (a) interest rates, and (b) greater supervision. Or was it the thinking of the commission that regardless of any other considerations, and any action that might be proposed by government, the ceiling on interest rates must come off?

Mr. GIBSON: Well, Mr. Lambert, I think the last statement that you made correctly describes the situation. I quote from page 364 of the Royal Commission's report, in the second column of the last paragraph, it says:

We recommend that it—

That is, the 6 per cent ceiling on interest rates.

—be removed regardless of other changes in the legislation.

There is no qualification for that "regardless of other changes in the legislation". Let me go on to say this: that the report did hope that a lot of other things would be done too, and that we could get a logical package, as you say. But the commission certainly felt, and I think this wording suggests that it felt it very clearly, that the ceiling should be removed regardless of anything else.

Mr. LAMBERT: Thank you, Mr. Chairman.

(Translation)

The CHAIRMAN: I will now give the floor to Mr. Clermont.

Mr. CLERMONT: Mr. Gibson, you were a member of the Porter Commission. You will remember that one of the main recommendations you had made was for an increase in competition between the banks and other institutions within the banking system.

(English)

Mr. GIBSON: Yes, sir, I would say that was one of the main recommendations.

(Translation)

Mr. CLERMONT: In your brief, Sir, do you say that C-222 will provide more competition among the banking institutions generally?

(English)

Mr. GIBSON: Yes, Mr. Clermont; I do believe that.

(Translation)

Mr. CLERMONT: Do you feel that the removal of the interest rates will bring this about? You also propose the "removal or lessening of restrictions on banks to compete—in its approach to the interest rate ceiling, in its differential treatment of reserves against demand and notice deposits, and in its provision for more rapid entry of the banks into the mortgage business." Do you feel that the removal of the interest rate will make funds more readily available for medium or small, scale industry?

(English)

Mr. GIBSON: Yes; I do believe that the removal of the interest rate ceiling will, in time, make funds more available at lower rates than otherwise would have been the case for medium, and small scale business. I qualified my remarks, sir, to the effect that money was very tight now, and it just would not be logical to expect a very rapid response in these circumstances.

(Translation)

Mr. CLERMONT: Do you feel, Mr. Gibson, that if this legislation as introduced here allows the banks to go into the mortgage field or into N.H.A. loans, that the banks, as suggested by Mr. Lambert, would be rather inclined to make loans in that area than commercial loans to medium or small scale businesses?

(English)

Mr. GIBSON: Well, Mr. Clermont, one can only give views as to tendencies here; I cannot give you a black and white answer. I think that banks, depending on their feeling about what they are best at, would tend perhaps toward the mortgage business, or perhaps more toward the lending to small and medium sized businesses. These two fields tend to overlap very much. If you are making a term loan to a small type of business it often tends to be a mortgage loan. Usually mortgage security is taken in this kind of a loan, so that I would not think of these two possibilities as being entirely in competition with each other. The conventional residential mortgage lending could very well be in competition with making term loans to small businesses. But I would think it would depend on the bank, what they think they can do best. As I said earlier, most of the banks have a very substantial branch system, they are spread across this country; they want to do business with, and support the small businesses in their areas, because there is the branch, it has got to do business, the man is trying to develop it. Most of the businesses in small communities are small businesses, so he wants to develop this business. I think you would find a strong tendency in this direction.

(Translation)

Mr. CLERMONT: When banks went into the mortgage field from 1954 until 1959, do you have an idea of the actual percentage of such loans that were made in proportion to the depositors they had? I believe that if the present plan is adopted banks will be able to go up to about 10 per cent progressively?

(English)

Mr. GIBSON: Yes, over five years, I think, sir. I do not have those figures at hand. My recollection is that it went up quite quickly from 1954 to 1957. But I

would just be guessing if I gave you figures; it was not a very high percentage, maybe 5 per cent or 6 per cent.

Mr. CLERMONT: Would it be 10 per cent, or below 10 per cent?

Mr. GIBSON: Below 10 per cent.

*(Translation)*

Mr. CLERMONT: On page 4 of your brief you state: "There must always be new candidates ready to move in when the older and larger businesses show lessened vitality and efficiency". Did you have anything particular in mind? Do you feel that banks could possibly be replaced by other institutions?

*(English)*

Mr. GIBSON: Well, certainly, Mr. Clermont, by other banks. There are a lot of financial institutions which are fairly close to being banks. In the report of the Royal Commission, we envisaged the day when perhaps some of the trust companies might formally become banks, and that this would widen the competition in the banking area.

*(Translation)*

Mr. CLERMONT: I want to explain the why and wherefore of my question, Mr. Gibson. This Committee and Parliament have studied requests for the setting up of these two new banks, that concerning the Western Bank in one instance whose charter was approved by Parliament, and another request put forward by a British Columbia group asking for a charter to operate under the name of "Bank of British Columbia". This Committee put certain recommendations forward in this regard and these recommendations have come back from the House of Commons and the Senate. That is why I wonder how we should interpret this statement on page 3. Mr. Coyne, the former Governor of the Bank of Canada, gave us to understand, if I remember correctly, that there is room in the Canadian economy for the establishment of six, seven, eight, or even ten new banks, especially regional banks.

*(English)*

Mr. GIBSON: I find that difficult to answer; I would not disagree but I just do not know, sir. This is a very difficult question.

*(Translation)*

Mr. CLERMONT: At the outset of your brief you seem to suggest a greater degree of competition between financial institutions. You seem to say that under the present Act, as amended in 1954, the banks were discriminated against, that they could not compete as freely as they could have otherwise. And I would return to this Act. That when these two groups were asking for new charters, we had evidence before us that banks had advantages over the near-banks, in a great many areas. Would you share that point of view?

*(English)*

Mr. GIBSON: I do not think so, Mr. Clermont, but I would like to know more specifically what you are saying to get a clear idea of the point you are making.



(Translation)

Mr. CLERMONT: In the Bankers' Association brief and in your brief, you state that near-banks enjoy advantages over you in a number of areas of activity. They can for instance attract deposits more readily than banks. The near-banks however claim that you have other advantages over them. I would like to know your views on that matter, as an ex-banker and economist and member of the Porter Commission? What are, according to you, these advantages which the banks would have and which the near-banks would not have, apparently?

(English)

Mr. GIBSON: It is much easier for me, because of my background, to say what advantages the near banks have over the banks. I think I made that fairly clear in my brief. They are not limited or restricted to a 6 per cent interest rate ceiling; they are not required to keep certain cash reserves, and, in some areas of business where the banks would like to operate, they are free to operate and the banks are not; I am referring specifically to the area of mortgage business and taking mortgage security.

Now, looking at it from the other side—I do not think you are asking the right man this question, I am sure someone else could answer it better than I could—the near banks, in some cases, are not permitted to make what we would call business loans; they are not permitted to make unsecured loans, personal or business. This is a real disadvantage, and the Porter Commission recommended that they be allowed to do these things. We felt that they should be given basically the same rights as the banks. I do not know that I want to go much farther than that, sir. I think a near bank would tell you that most of the banks are bigger than the near banks, because they are bigger perhaps size has some advantages in this world.

(Translation)

Mr. CLERMONT: Mr. Gibson, are you satisfied that under C-222—

The CHAIRMAN: Mr. Lambert I believe, was to raise a point of order. I believe we are in agreement that we should discuss this matter of interest rates rather than anything else.

Mr. CLERMONT: At the outset you had apparently said that reserves and interest rates were to go together?

The CHAIRMAN: I had agreed with Mr. Gibson on an order.

Mr. CLERMONT: I think I understand your point of view. My questions on interest rates or the removal of interest rates are concluded.

The CHAIRMAN: Thank you, Mr. Clermont.

(English)

Now I recognize Mr. Cameron.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Chairman, I should like to go back to the question Mr. Clermont was raising, namely whether Mr. Gibson thinks that the removal of the ceiling will cause the banks to extend credit to—I think Mr. Gibson's words were that they have been restricted, and discriminated against—in such a way that they have not been able to extend

credit to certain elements in the community, and his hope was that with the removal of the ceiling, they would be able to do so. Now, in light of what Mr. Gibson said—and I think this is very wise—that we should consider this proposition, not on the basis of whether the banks are good fellows or not, but whether it will serve their interests to take a certain course of action—the question I would like to ask is this: do you see the possibility, Mr. Gibson, of the banks being able to extend credit to these hitherto discriminated against sections of the community by means of the removal of the ceiling; that their interest of making profits, that is their business, can be served in such a way that by raising interest rates they will overcome the difficulties regarding smaller borrowers in the way of more cost in supervision of the loans, and so on. Is it possible that interest rates can be raised to such a degree that it will make such loans equally desirable as loans to larger borrowers in which the element of the cost of supervision in relation to the size of the loan is much less; do you think it may be possible to do this?

Mr. GIBSON: Yes, Mr. Cameron, I do, in time. I qualify my view, though, in a statement I made earlier, that money is very tight today, and that it would be difficult for most banks to expand their loans in any direction; they are having trouble looking after their regular customers. But this is not a normal state of affairs, and looking a reasonable distance ahead, I would expect the banks, given freedom to charge rates that would give them a margin of profit, to develop this field, for the reasons that I gave earlier, that they have this branch system which goes pretty well all over the country, and they have the men that are trained to do these things, and branch bankers think of themselves as members of the community. This is sort of added to the way they develop, and the way they work; they want to support business enterprises in the community. The area where I think the serious deficiency is, is in the sort of medium term, longer term loans to small businesses. The banks already lend a great deal of money on a short term, working capital basis to the bulk of businesses in Canada. Really the problem that we are talking about here, I think, is whether they would get a bit farther into the field of term lending to smaller and medium sized business, with the hope that this would have the broad economic effect of helping more of the smaller businesses grow into bigger ones. I think, as I said in my brief, this is extremely important for the welfare of this kind of society, which would have new people coming up all the time.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But you feel that this is not likely to take place during the present tight money conditions; is that right?

Mr. GIBSON: I would be very surprised if a great deal happened under the present extreme conditions of tight money.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): In light of the world wide shortage of capital, do you see any prospect in the next five, six, or seven years of there being any great decline in interest rates?

Mr. GIBSON: That is a very difficult question, sir. I would hope that interest rates would not go much higher, and that they might go down a bit. I agree with what I think is the implication of your remarks, that is, that there is a shortage of capital in the world. It is hard to see this disappearing in the near future. I think it is somewhat accentuated now, and the problem of tight money is not

just a problem of interest rates; it is a problem of the degree of—one of the phrases used is degree of heat in the economy; whether you are generating much inflationary pressure.

You can have easier money, and still have quite a lot higher interest rates than we have been accustomed to. The point I am trying to make is that I think the present situation is one of inflationary pressure. So long as this lasts you are going to have tight money in every sense; but when it eases you may still have higher interest rates than we have been accustomed to in easier times. But you have more money available, and this might mean some modest reduction in interest rates, but I would not look to a great reduction in interest rates.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): On what do you base your suggestion that there will be a larger supply of money available, or that there may be within the foreseeable future?

Mr. GIBSON: I base this view on the opinion that the present state of inflationary pressure will not continue indefinitely. It will ease one of these days, and then the monetary policy will be less tight, and there will be more room; you will get more competition in your financial system then. People will be beginning to look for loans, looking for opportunities. But with money as tight as it is, this is not the case; they have to look after their regular customers, and there is not much left over, if anything.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Do you think that even in a situation where there would be an increase in the money supply, accompanied, as you have suggested, possibly by a continuation of high interest rates; that in those circumstances the banks will be able to move into these fields, or would move into these fields?

Mr. GIBSON: Yes, I do, sir. I do not want to suggest that I think interest rates are going to stay at current levels indefinitely; but I do think it is quite possible that we are not going to see them going back to the kind of levels that we were accustomed to seven or eight years ago. You might get some reduction, but not the sort of level that you might like to see.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): In view of the increasing volume of economic opinion that we have moved out of the period of inflationary pressures, if one accepts this view, which is contradicted in other quarters, but seems to be a growing opinion among economists, that our period of inflationary pressure has passed, would you foresee a decline in interest rates, or how soon would you expect to see any such decline? Put in another way, do you foresee a relaxing of the pressure forcing interest rates up, in the near future?

Mr. GIBSON: Yes; I would expect some relaxing of the pressure, but I would not associate myself with the view that the view that the inflationary pressures have passed. It seems to me there is a good deal of evidence that a lot of them are still very much with us. Therefore, I would not expect a great deal of easing in the near future.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): In effect, in the circumstances that you foresee for the foreseeable future, we are not likely to see much change in the ratio of the banks credit-extending facilities, they will be following much the same pattern they are following now and have followed for some years.



Mr. GIBSON: Well, Mr. Cameron, I would not say the foreseeable future; I said the near future, and I would not expect much change in the near future. You, after all, are talking about a bill which, when it goes into effect, will be in effect for 10 years, and I would expect a lot of changes in 10 years. I would expect a good deal of action in the direction that we were talking about earlier, namely, the development of term loans to small business, and the development of the mortgage business. But I would not want to say when that is going to happen; I am afraid I do not have that kind of foresight.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Thank you, that is all now.

The CHAIRMAN: Now I would like to recognize Mr. Leboe.

Mr. LEBOE: Thank you, Mr. Chairman. I would like to ask Mr. Gibson if he would care to comment on whether he feels that in dealing with our banking legislation, we are dealing with it in a state of isolation from other pertinent facts as far as the welfare of Canadians is concerned. I am referring, not to the specific, but to the general economic condition of Canada, which is influenced by many more things than banking. I am wondering if you would care to comment on whether we are not dealing with this particular matter with too much isolation in our thinking?

Mr. GIBSON: I could not answer that question, Mr. Leboe, because I do not really know. I am not close enough to the discussions of your Committee, but I suspect from what I have been hearing this morning that you have been looking at this from the standpoint of a pretty broad canvas. I am not sure that I understand your question.

Mr. LEBOE: Perhaps I could add something here to clarify what I am really getting at. Are there any other methods, in your mind, that are increasing the service to small business other than the increasing of interest rates. In connection with that, I do not see how the increase in interest rates is going to increase the total money supply. If the small businesses get certain amounts of money that they did not get before, then other people are going to have less money if the total money supply remains the same. I am wondering whether you think there are any other methods of increasing this service to small businesses, other than increasing the interest rates; I certainly feel that there are, and this is why I asked the question.

Mr. GIBSON: There are several points that you raised. You suggested that if small business got more money, as a result of the banks being free to charge more economic interest rates, then there would be less money available for other people. I do not know that this follows. The Bank of Canada, as I understand it, carry out their policies affecting the money supply in the light of the state of credit conditions; it is not a rigid money supply approach, as I read it. From what the governor says from time to time, he is not just looking at a figure of how much money supply there is and how the economy looks at the time. He is looking at the general state of credit conditions, of interest rates, the availability of money, and so on. All I would say to that point is that it would depend on the circumstances. It might be appropriate that there should be an expansion of the term kind of credit that I have been talking about, and the deposits which would finance part of this would attract a smaller cash reserve requirement under this

proposed bill. I do not think one can conclude that development in banking business in this area would necessarily mean that funds were taken out of other areas.

Mr. LEBOE: You are saying then, that the Bank of Canada, by its policy, would increase the reserves to the banking system. And we are talking about banks now and not near banks, although near banks would be affected as well. They would increase their reserves to the chartered banks, so that the result of the higher interest rates would be that they would tend to give loans to smaller businesses. The Bank of Canada, by the increase of their reserves, would then provide more money available for loans to other businesses, which are the traditional borrowers at this moment.

Mr. GIBSON: I could not say what they would do; I do not know. It does not follow, however, that more loans in this particular area would mean less loans in other areas. It would depend on the circumstances; the Bank of Canada would judge what it thought was appropriate in the given set of circumstances.

Mr. LEBOE: If the Bank of Canada did not increase the reserves, then what we would really be doing is actually transferring loans from the conventional borrower now to longer term loans to smaller businesses at a higher rate of interest. Is that what we are really proposing here, if the Bank of Canada, through its money policy, did not make more money available?

Mr. GIBSON: Yes, Mr. Leboe, but I cannot envisage this as happening, because the banks, first of all, are going to look after their regular commercial customers. They are not just going to take money from them and hand it off to somebody else. More than that, it seems to me, over a period of time, the Bank of Canada is in fact going to expand credit; the central bank always has to expand credit over a period.

Mr. LEBOE: That is right.

Mr. GIBSON: It is a question of how much, and I cannot tell you how much; it depends on the circumstances, and their judgment in light of those circumstances.

Mr. LEBOE: This is the answer I was looking for, because I want your views on the matter. Now, this is a related question having to do with finance companies which are controlled by the banks. I might preface my remarks by the experiences that other people have had, and I am sure that you are aware of these; when there is a tight money policy going into effect, it is known to the finance companies previously to the information being passed on to the general public. They are asked, deliberately, to increase their line of credit, against the day when the tight money policy will be brought in. The result, of course, is that person (a) comes to the bank and says "here is my statement"—and it is a very good statement—but the bank says "we are on a tight money policy". So, what actually happens is the individual then is sent—and I know this to be a fact—to a finance company. Now, the finance company has previously raised its line of credit at the bank, making it available to him; but the other unsuspecting individual has not raised his line of credit. I could actually cite places, and names in connection with this, so I know what I am speaking of. The fact remains then, that the individual, instead of getting his money at the bank rate, walked across the street, or down the street two doors, picked his money up at a finance

company, and paid up to 24 per cent interest; and all the finance company did was to turn the paper over to the bank against the line of credit that was established. The bank loaned the money to the finance company to loan to the individual, when he should have got it from the bank in the first place. I would like to know from you, Mr. Gibson, as a banker for many years standing, I take it, and as a member of the Porter Commission, your views in connection with some sort of—I do not like the word control—system, whereby this type of thing could not be foisted on the unsuspecting public.

Mr. GIBSON: Well, Mr. Leboe, in my banking experience, I certainly have not run into many cases of the kind you describe. Banks, of course, do give lines of credit to finance companies, but they are not inclined to increase those lines when money is tight. Indeed, the finance companies have made a great deal of complaint to the effect that the banks have been inclined to cut them back. Certainly, in my banking experience, this has been the tendency, that we have felt more and more, when money is tight, that we are not going to provide stand-by lines for people who do not necessarily use that amount at other times.

My general impression would be that finance companies found it increasingly difficult to get large lines of credit, big lines of credit, from the banks. Of course they had lines, but as we found in our investigation, and this report, the bank credit was playing a decreasing part in the financing of finance companies in recent years. Finance companies in very recent times, have had more difficulty in floating paper in the short term money market, as you know. They have come back and tried to get more money from the banks, but I do not think they have been very successful. I think the banks help businesses, when they very much need money, but certainly, it would be my impression, that bankers, being in competition, to a degree, with finance companies, from a longer range point of view, are not going to fall over backwards to finance them; they are more interested in doing the financing directly. This is my personal view; I am not speaking for the bankers.

Mr. LEBOE: From what you have said, I gather that you believe that this situation is on the way to being improved from what it was some few years ago. The finance companies have an insatiable appetite for money. I think you will agree with this, and they go out and get it wherever they can get it.

Mr. GIBSON: Mr. Leboe, anybody has an insatiable appetite for money, particularly at 6 per cent.

Mr. LEBOE: Actually I am trying to assess this situation. I would like to think of some other means of getting these loans to the small businesses, other than by raising the interest rates. We do have, in many other types of our economy, certain measures that have been taken. For instance, a trucking firm has a charter; no other person can take goods from (a) to (b), only that one trucking firm. The reason for this is so that they do not get into a starvation competition, is that right? I am wondering whether we should not take a look at this whole problem in a broader sense, to find out whether we could not supply money to these smaller businessmen on a term basis, profitably as far as the financial institutions are concerned. I think, for instance, you find a very large bank building on a corner of a street, and almost on the next corner you find another branch of the same bank; all that happens is the individual does not have to cross the street, he can do his business on one side of the street instead of



the other. We have complaints now, and I think justifiably so, that in many towns we have too many service stations selling gasoline, which pushes the price of gasoline up. I think that one of the Royal Commissions indicated that this was so and they recommended a curtailing of the number of service stations in a given community. I am wondering whether there is not another area in the banking business that we should be looking at very critically to find out if it is possible to keep the interest rate at a low rate to these small business people; and I think there is. I am wondering if you have any comment on that?

Mr. GIBSON: Well, Mr. Leboe, I share your desire to keep the interest rate to the smaller businesses, and indeed everybody, as low as possible. But one has to pay the cost of money at a particular time. The fact of the matter is that today even short term money costs the bank  $5\frac{1}{2}$  per cent plus—and I know the bankers will say I am away low on that—if they want to go out and get it now. The money on the books, of course, does not cost as much as that because they have a lot of money accumulated over the years in savings deposits, and some in demand deposits. But if you are looking for additional money, and if you are going to expand term loans to small business; you have got to look for additional money. Money is expensive, and as I say,  $5\frac{1}{2}$  per cent would be a very low statement of the additional cost of short money, very short money. If you are thinking of longer money, it is more expensive than that again. Now, if the banks are going to go into this business, they have to pay the cost of money; and they have to get a spread on it. What I have been saying is that I think they can do it cheaper than almost anybody else. Because they have the equipment and the staff to do it. If you try to get somebody else to do it, they are going to have to build up the equipment and the staff, and my guess is that it is going to cost you more; because things cost more these days. These things already exist, so far as the banks are concerned.

I do not say short term money, or long term money will always cost as much as it is costing at present. I expressed the view to Mr. Cameron that interest rates, the way things look, may not go back to the sort of levels we thought were customary not so many years ago; but I do not think they will necessarily stay up where they are now. Therefore, I do not think one should draw the conclusion that the costs to small business money are going to be very high. I think this is the cheapest way of getting more money, over a period of years, to small businesses. I think the banks can do better than their competitors in this area.

Mr. LEBOE: Well, I certainly feel that I can agree with you 100 per cent on the fact that the banks are in the position to do just exactly that: to service the people better in this area than any other financial institution. This brings me to my last point, and that is: do you believe that what we call near banks must be put in the position—I mean through legislation—of some sort of control where not only are their financial operations—and now I am thinking about several companies which have been in trouble, and are in trouble, financially—going to be more secure, and their deposits are going to be much more secure, not particularly from the point of an insurance program which was suggested will be coming in, but from sound financial practices. And I am thinking about all the gimmicks they have to have people come in and put money in their hands to be loaned out. According to the information gathered by this Committee, they are not required to keep, in some cases, adequate reserves. I am thinking now of a much sounder financial structure, because it is my opinion—and I would like you

to comment on this—that the whole business of money lending, and the receiving of deposits, has got out of hand almost to the state of confusion in the business. However, I did not want to put you on the spot.

Mr. GIBSON: No, sir; I agree. I think more good supervision is necessary in this area. It has got to come from two directions; one, is better securities legislation—and we are making some real progress here—and the other is better regulation of deposit taking institutions. I have expressed some views here; the essence of this is good supervision. Now, you have before you in this bill a proposal of trying to get there via the route of deposit insurance and dominion-provincial co-operation.

The CHAIRMAN: It is not actually in the bill.

Mr. GIBSON: I am sorry, Mr. Chairman, it is not in the bill, but it is associated with the bill, and the Minister has made reference to this question. This is one way of approaching the problem. I am not too confident that it is going to work effectively, but it may. Our commission had a different approach. We felt that there was a great deal to be said for defining banking, and trying to regulate people who did banking; this was thoroughly within the federal government's powers. But maybe from a practical point of view, there is a good deal of merit in the other approach; I do not know, I would not like to express a view on this. All I would say is that the situation obviously needs improving; it is not good enough.

Mr. LEOE: I would just like to thank the witness, Mr. Chairman, for his co-operation.

The CHAIRMAN: Mr. Gibson, perhaps at this point I might ask you something arising out of Mr. Leboe's comments about the cost of borrowing, and so on. It has been clear to many members of the Committee that in recent years there is a growing use, by the banks, of the technique of the compensating balance and the service charge, in addition to the interest rate, which they are asking borrowers to pay. If the interest rate is freed, along the lines of the recommendations of the Porter Commission, what justification would there be for a bank to charge a borrower a service charge, and to also ask him to maintain a balance greater than the ordinary working balance in his account, in addition to the interest rate that would seem to be justifiable in the circumstances?

Mr. GIBSON: Mr. Chairman, I have been out of banking for a while.

The CHAIRMAN: Not that long.

Mr. GIBSON: Well, perhaps not, but from reading the evidence I see there has been a certain amount of discussion about this. The service charge and compensating balance are related to the cost of providing various services. If you speak of what justification there is to charge a borrower, purely as a borrower, then I could not support this. I would say that the compensating balance is for the purpose of covering costs of providing services; it is not part of the interest rate. That is certainly the way it was when I was around.

The CHAIRMAN: As I drew to the attention of the bankers, when they were with us, in their submission to the Porter Commission, they suggested, and I will quote here:

Only when compensating balances are in excess of ordinary working balances would the cost of bank credit to borrowers be raised, but this can

be achieved more simply through higher interest rates which are to be preferred because they state precisely the cost to the borrower.

In making a submission to the commission they seem to make the compensating balance in the circumstances, referred to in the statement, an equivalent to interest rates. I was interested to note in looking over the Porter Commission Report, that nowhere in your report, did I notice any reference to other costs to the borrower, other than the interest rate. In fact, the only reference that I noted covering costs other than the cost of the money, was on page 364 of the report, where the statement was made that:

The ceiling stands in the way of flexible lending by the banks in that it frequently prevents them from making loans on which higher rates must be charged to cover administrative costs and risks.

Mr. GIBSON: I cannot speak for what has been going on in this very recent period, but certainly when we wrote this report the question you raise was not a live question at all.

The CHAIRMAN: I felt that you might be in a unique position, without giving away any confidential information, to inform the Committee on this issue which is of more interest to the public at this time, particularly with respect to what will happen to the borrowing customers of the banks if the proposals of the commission are adopted with respect to freeing the interest rate, either in the form the commissioners recommended, or in the form in the bill before us. Would it not be possible, or, in fact, preferable to permit the borrower to know the total cost of his borrowing in the form of an interest rate, rather than charging an interest rate plus a balance above that required to maintain his account plus service charges on his cheques, and other items?

Mr. GIBSON: I think you should ask the bankers about this, because it does not really conform with my experience.

The CHAIRMAN: We did have some discussion with the bankers, and when you say this does not conform with your experience, you mean that your experience has not been to require all three items to which I have referred?

Mr. GIBSON: That is correct. In any event, in my experience balances have not been considered as part of the interest rate structure, at least as an alternative of the interest rate structure.

The CHAIRMAN: But a balance in excess of the working balance in the account, is, in effect, an increase in the cost to the borrower for the use of the funds.

Mr. GIBSON: That is right. It is a question of what you need the increased revenues for, whether you need it to provide service, or whether you need it for other purposes.

The CHAIRMAN: From the point of view of the borrower it is part of the total package of cost.

Mr. GIBSON: If he is solely a borrower, and if he is not getting any other services than borrowing services, that would be so; it usually is. You have me in a difficult position here, because I am really not up to date on this story.

The CHAIRMAN: What was the practice when you left?



Mr. GIBSON: This was not a major issue.

The CHAIRMAN: That was a year ago.

Mr. GIBSON: A little over a year ago, yes.

The CHAIRMAN: Would you be surprised if I told you that at least in my experience it seems to have become a major issue with a number of bank customers?

Mr. GIBSON: I have heard rumours of this, Mr. Chairman.

Mr. CLERMONT: I have a supplementary question, Mr. Chairman. Why are you making a difference between a borrower account, and a non-borrower account, on services charged to them.

The CHAIRMAN: Why am I making a difference?

Mr. CLERMONT: Yes, why?

The CHAIRMAN: Well, I presume, in fairness to the bank, that there might be people who do not borrow money from the banks, and they are using an account for the purpose of having cheques go in and out, and so on.

Mr. CLERMONT: Is that not the same with a borrower's account? Is he not issuing cheques?

The CHAIRMAN: He may in the sense that he is using his own funds, rather than funds that he has borrowed from the bank.

Mr. CLERMONT: But if he borrowed money from the bank he received something; he received money. Why should a non-borrower account be discriminated against concerning bank charters?

The CHAIRMAN: That is exactly what I am suggesting. I am trying to distinguish between the fellow who has come to a bank and received a loan, for which he is charged a rate of interest.

Mr. CLERMONT: Yes, but you see he is getting something when he applied for a loan; regarding the rate of interest, if it is 6 or 6½ per cent, he is getting a loan; he is getting money. Why should this borrower not pay any bank charges on the transaction of his account?

Mr. LEOE: I would like to ask, Mr. Chairman, who is the witness here?

The CHAIRMAN: Well, that is a useful question. We will have an opportunity to pursue this further, but I might say that I think that the issue concerning some is that it would be useful for the customer to know clearly the total cost of receiving his money and using the services of the bank. Also, because there are bank customers who have the idea that some of the things they are being asked to do now are in lieu of a higher interest charge, and if we propose to parliament and parliament accepts the recommendation to free the interest rate, these charges will disappear.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): We had no assurance of that from previous witnesses.

The CHAIRMAN: No, and I think we should draw that out. If they cannot give us the assurance, the public should be aware of this.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): They were unable to give us any assurance.

The CHAIRMAN: I thought perhaps Mr. Gibson, because of his unique position of having very recently ceased the active practice of banking, might be able to inform us further. In any event, I think it would be appropriate to recognize Mr. Laflamme.

Mr. LAFLAMME: Mr. Chairman, my question is precisely that question of service charges. When we had the bankers here, they said that they had forms showing the borrower the total cost of his money. If the ceiling is completely removed, is there any significance in having service charges added to the interest rate? I think this question has to be cleared up.

Mr. GIBSON: I agree with you that the borrower and the other customer ought to know what he is paying, and for what; this is right. This is a very complicated question, particularly the compensating balance one, because people have been tending to cut down the balances that they have carried over the years with the banks. The banks have found that the lack of working balances that they have been getting, has been an additional cost factor, or they were not getting the revenue from that source that they normally would have expected to get. So, whenever they can, they try to persuade the customer to keep a larger working balance. I cannot really go much farther than that; I am not in the banking situation now. I do agree with you that the customer should know what he is paying for.

Mr. LAFLAMME: On his interest cost; because we have been told that the service charges are legal, and if the banks are allowed to ask for a service charge in addition to the interest rate, I think they are, in effect, evading the effectiveness of the bill.

Mr. GIBSON: That depends if the service charges are being charged for services that have been given.

Mr. LAFLAMME: They are free to impose them to compete with the others.

The CHAIRMAN: You mentioned the necessity of asking the customer to maintain working balances, but what about asking the customer to maintain a balance in excess of what the bank considers necessary as a reasonable working balance, and also, at the same time, asking for service charges on items going in or out of the account; is that reasonable?

Mr. GIBSON: Well, there has to be a reason for it, sir. I agree with you, that you do not do these things for nothing.

The CHAIRMAN: If the customer in our banking system, say at the present time, does not like this type of treatment, assuming that is the treatment he is getting, what do you suggest he do about it?

Mr. GIBSON: I do not really think I could answer that. That is a very hypothetical question, you see; you assume that a certain thing is happening to the customer, and I do not really know the story.

The CHAIRMAN: Well, assuming it is happening.

Mr. GIBSON: What does he do about it?

The CHAIRMAN: Yes.

Mr. GIBSON: Well, I suppose he protests.

The CHAIRMAN: And then?

Mr. GIBSON: Well, I do not know, sir.

The CHAIRMAN: That is very significant that you give this answer, because we are told by the bankers that the banks are competing between themselves. Therefore I would have thought you would have said that he should go to another bank; but you did not say that; that is a very significant thing to me.

Mr. GIBSON: Obviously this is the thing, that any customer can always go to another bank.

The CHAIRMAN: What would happen then?

Mr. GIBSON: It is perfectly clear also, that when money is extremely tight that customers do not tend to leave banks; they want to have what line of credit they have got, and they know the other banks are tight, too. I think this is just a fact of life.

Mr. LAFLAMME: Mr. Gibson, is it a fact that when this bill comes into effect it will not increase the money supply for the public?

Mr. GIBSON: The passage of Bill No. C-222?

Mr. LAFLAMME: Yes.

Mr. GIBSON: I do not think it has to do with the money supply, sir. I think it has to do with the regulation of banks under the Bank Act, what parliament regards as their proper behaviour. The amount of money supply lies in the hands of the Bank of Canada.

Mr. LAFLAMME: When you say at page 3 of your brief:

The raising and ultimate removal of the interest rate ceiling envisaged in the bill before you will gradually make more funds available for small and medium sized business and because of the added competition will reduce average rates to the important group of borrowers concerned.

Mr. GIBSON: Yes.

Mr. LAFLAMME: So, how could they make more funds available for small and medium sized business if the money supply is not increased.

Mr. GIBSON: As I said, Mr. Laflamme, the present situation is one of extremely tight money. I would not expect very much to happen so long as money is as tight as it is right now; I would not expect that to continue indefinitely. It would seem to me that a time will come, perhaps not very far in the future, when money will be less tight, and the process that I describe as desirable, and I think likely, could then proceed.

Mr. LAFLAMME: I have only one further question, Mr. Chairman. When you say that the added competition will reduce average rates, do you mean by average rates the total rates of all the financial institutions? Then the interest rates charged by banks have to increase? And if they go into the fields of the others, then the average cost of the others would be reduced; but in any case the total interest costs will rise?

Mr. GIBSON: No. If you allow money to move freely, where it was not allowed to move before, if they are allowed to seek the best return they can get



for money—and they were not allowed to move into that area before—you get a freer movement of money, and, I think, a lower rate than otherwise would have prevailed. The situation you have now in a lot of the area of small business is that certain companies do provide funds; some of the rates are very, very high. I think the banks would provide funds at a much lower rate than some of the present providers of funds, but higher rates than the banks charge now. I think the average cost of money to this group would tend to be lower than it otherwise would have been.

Mr. LAFLAMME: It means then that the average cost of the banks will increase, and the average cost of the other financial institutions will be reduced.

Mr. GIBSON: Yes, the banks would charge more than they are charging now because they are not lending a great deal of money in this field; there is not enough in it to do so. The competition, presumably, would narrow the field for other lenders who are now in it. Whether they would come down much, is a matter of time. I think it is true that when the banks got into the field of personal financing they did bring about, through their competition, a reduction in the average charges that finance companies made in that area, over a period of time.

The CHAIRMAN: Thank you, Mr. Laflamme. I think that now would be an appropriate time to recess the meeting.

*(Translation)*

It is possible that this afternoon your Chairman will have to be present at another Committee. I would therefore ask the Vice-Chairman to take the chair so the meeting is now recessed until this afternoon.

*(English)*

Mr. ADDISON: Mr. Chairman, I do not know how quickly our meeting will gather momentum, but I would like to ask Mr. Gibson later on, if at all possible, about the section on foreign control of Canadian banks. Unfortunately, or fortunately—I do not know which—I am going to Detroit with the Justice Committee at 7.30 p.m. to find out what makes automobiles tick. So, if we do not arrive at that, say by 5.45 p.m., would it be possible for me to pose some questions to the witness?

The CHAIRMAN: I would think so, and it may very well be that we might make the suggestion that we take this topic out of the order in which it is presented in the brief, so that we could have a general discussion of it, and your questions will not be in isolation. Perhaps we will consider that right at the opening of the meeting this afternoon; I think that might be a better way to do it.

Mr. CLERMONT: Mr. Chairman, I am sure you have taken into consideration that something may happen in the House of Commons.

The CHAIRMAN: Well, we also have to take that into account, and it may well be that our meetings will not be as extensive as might otherwise have been the case.

#### AFTERNOON SITTING

The VICE-CHAIRMAN: Order, please. I have a list of those people who wished to ask questions of Mr. Gibson. First I will recognize Mr. Gilbert on the first topic which is interest rates.

Mr. GILBERT: Mr. Chairman, this morning Mr. Gibson stated that the 6 per cent limitation that was imposed on the banks acted as a restriction to the competitive aspect of the bank's business. He also stated that the Porter Commission recommended its immediate removal, regardless of other changes. I am wondering, Mr. Gibson, if the 6 per cent limitation had any effects on the profits of the banks over the years because in this morning's *Globe and Mail* there appears a report on the profit of the Toronto-Dominion Bank, which reads:

Reported profit of Toronto-Dominion Bank was a record \$10,892,656 or \$3.63 a share in the year ended October 31.

This was 9.9 per cent higher than the 1964-65 profit of \$9,914,543—which was 9.2 per cent above the previous year's.

In other words, over the past two years there has been an increase of 20 per cent with regard to profit of the Toronto-Dominion Bank. Would you say that the 6 per cent limitation has had a bad effect with regard to the profit position of banks generally?

Mr. GIBSON: Mr. Gilbert, I do not know. The annually reported profits changes for the banks are part of the story. Part of the story, of course is how much of a return they are making on their capital and whether or not they are attractive places in which to invest additional money, and whether they are attracting enough money or putting away enough earnings to cover their expansion. My own guess is that if they were freer and had a more competitive system they might do better. They might be bigger but they would provide services more efficiently to the Canadian economy. I just could not tell you whether their profits would be larger or smaller. It is quite possible they would be somewhat larger. If they did the job better, if they had a bigger volume, this makes sense. They might be attracting more money; they might be increasing their capital more rapidly than they are. To increase capital you have to make enough profits to carry it.

Mr. GILBERT: Would you agree that one of the methods the banks use was the consumer loan which has a net interest rate of roughly 10 per cent or 11 per cent, and they thereby avoided the 6 per cent limitation. So you had the aspect of services charges and compensating balances. Are not these methods that the banks employed to overcome the 6 per cent limitation imposed by the act?

Mr. GIBSON: Well, with regard to consumer lending, it is correct, as you say, that the finance charges come out to—I have forgotten the exact figures—I think between  $9\frac{1}{2}$  per cent and  $11\frac{1}{2}$  per cent. This is the kind of range. This consists partly of interest and partly of service charges. The banks have gone into this field because it is an interesting and profitable field. This is quite correct.

Mr. GILBERT: I am not objecting to their going into it.

Mr. GIBSON: Oh, no. But this is the incentive. I agree with you that banks try to do things that will earn a dollar and I think this is the way they ought to behave.

Mr. GILBERT: I notice, Mr. Gibson, in the Royal Commission report that you dealt with the Small Loans Act and you will recall in the Small Loans Act there is a definition with regard to cost of a loan. In that definition is set forth what constitutes cost of a loan. If I remember correctly the Porter Commission recommended that the total cost of a loan be stated on a percentage basis. Now,

if we can do that with regard to small loans, is it possible to do it with regard to commercial and consumer loans?

Mr. GIBSON: Personally, I do not see why not. I would not object to this. But I would like to go back to your first question. You asked also if the banks were trying to "get around" the 6 per cent ceiling, or words to that effect, by requiring balances and something else.

Mr. GILBERT: Service charges.

Mr. GIBSON: And service charges?

Mr. GILBERT: Yes.

Mr. GIBSON: I would just like to say a word on that first. The service charges are not for lending money. The service charges are for performing services in connection with the activity of an account. The service charges for activity are related to the activity of the account, not whether or not it happens to be borrowing on a deposit account. Banks, and I think quite correctly so, do not regard this as having anything to do with the lending or interest charge.

With regard to balances, I am just not in a position to speak of what has happened in the last 12 months. When I left the Bank of Nova Scotia I spent six months working for the government of Canada out of the country and I have been trying to learn to teach in the university since. I am really quite out of touch with this but I can tell that when I left the bank sure, our bank and I think most other banks, were trying to persuade people to keep as large free balances with us as we could. This is a traditional practice in banking. Bankers like to have free balances. This is always the case. Bankers are always trying to get you to keep a free balance with them. You get credit for these free balances in terms of services charges. You do not pay both.

Mr. GILBERT: You probably noted, Mr. Gibson, that there is no definition of service charges in the Bank Act. Do you think there should be one?

Mr. GIBSON: I am sorry, I do not know.

Mr. LAMBERT: What is wrong with service charges?

Mr. GILBERT: Nothing, I am not suggesting there is. I think they should be set forth. I think there should be a definition of service charges, Mr. Lambert; that is all. As long as the borrower knows what the service charges consist of, I think—

Mr. GIBSON: It seems to me it would be possible to get a list of service charges for a particular bank. This is not secret.

Mr. LAMBERT: Mr. Chairman, may I intervene. Surely there is a confusion here that service charges seem to be limited to persons who borrow money from the bank. If Mr. Gilbert or myself maintained a current deposit account with any bank on which we write cheques we would pay service charges whether the deposit is on the basis of money we obtained through a loan or otherwise.

Mr. GILBERT: That is quite obvious, Mr. Lambert, what you have just said.

Mr. LAMBERT: Yes, but why this insistence that service charges should be related to some particular loan?

Mr. GILBERT: The best example—



The VICE-CHAIRMAN: I do not think I should allow discussions between members of the Committee. I think we should direct our questions to the witness who is presently here.

Mr. LAMBERT: But we are getting the same sort of confusion all over again, with the greatest respect.

Mr. GILBERT: There is no confusion on this side; I do not know why you are confused, Mr. Lambert.

The VICE-CHAIRMAN: Go ahead, Mr. Gilbert.

Mr. GILBERT: I will abide by your ruling.

The VICE-CHAIRMAN: No, I agree that since we have been discussing the interest rate which means, in itself, the total cost of money, I think the service charges can be discussed.

Mr. LAMBERT: I am not objecting to that. I am suggesting it leads to confusion in insisting on relating service charges to loan accounts.

Mr. GILBERT: I imagine Mr. Gibson knows what I am referring to. I think you have given your answer to it. You would have no objection to having the service charges set forth by way of definition and that in the Royal Commission report, I think they recommended that the total cost of the loan, which would include interest and service charges and whatever other charges are included, should be set forth on a percentage basis.

Mr. GIBSON: Mr. Gilbert I think there is some misunderstanding between us here. I agree with you that there are service charges associated with personal loans which make the interest rate at 6 per cent plus the service charge come out to the charges you have already mentioned and we have discussed. These are special charges in connection with personal loans and they are related to lending; this is true. But in the rest of the area I do not really see the relation of the service charge to lending. The rate of interest is 6 per cent, to the best of my knowledge. It was when I was with the bank, except in this personal loan field where we still find the rate of interest was 6 per cent but we had these additional service charges on top of that which brought the rates up to those we mentioned.

Mr. GILBERT: Are you suggesting then that the compensating balance covers service charges and service charges alone and does not include an added cost to the borrowing of the money?

Mr. GIBSON: The word "compensating" worries me a bit. I like to call them free balances. Banks like to get as large free balances as they can from customers. Sometimes the free balance may cover the service charges. Sometimes it may be equivalent to something more. I do not know. It depends on the circumstances. You introduce another idea when you say the balance is a condition of the loan. Frankly, I do not know about this.

Mr. GILBERT: It was not the experience of your bank at the time you were active?

Mr. GIBSON: No; we did our best to get as good free balances as we could. We did not make balances a condition.

Mr. GILBERT: Mr. Gibson, am I right in assuming that there are three main classes of loans; the commercial loans, the consumer loans and the mortgage

loans? If that is right, is it feasible, and again I am leaning on your experience as a banker, to have upper limits with regard to the interest rates chargeable. In other words, suppose an upper limit of say 10 per cent were placed on consumer loans, and an upper limit of say 7 per cent with regard to commercial loans and an upper limit of 8 per cent on mortgage loans, would that be feasible for the banks to operate in rather than have the limitation that is now proposed?

Mr. GIBSON: Whatever parliament decided, Mr. Gilbert, would be the terms under which the banks operated. I am sure they would operate to the best of their ability. The kind of thing you suggest does not appeal to me, if you ask my opinion. I think there is enough competition in this system to produce rates which are as favourable as they can be for the customer and induce the most efficient flows of money in the economy. The objection to the 6 per cent ceiling—leaving the interest of the banks out of it—from the standpoint of the economy, of the public, is that the resources are not allocated effectively. Some people do not get a crack at what is a big flow of funds that comes through the banks. If you just raise the ceiling a little, sure it will be better than it was because it will allow more of a margin and therefore a freer flow. But if you have as much confidence as I have in the competitive system I do not think you would worry much about the ceiling.

Mr. GILBERT: I think that is all, Mr. Chairman, thank you.

The VICE-CHAIRMAN: I will now recognize Mr. Flemming.

Mr. FLEMMING: Mr. Chairman, I have read Mr. Gibson's brief and I find it very interesting. The question which occurs to me at the moment is based on the premise that probably the most important single feature in the act that we are presently studying is the suggestion of an increase in the ceiling rate. I wonder if Mr. Gibson would agree with that general statement?

Mr. GIBSON: Yes, Mr. Flemming. I think either the increase or removal of the ceiling rate is the most important feature of the bill.

Mr. FLEMMING: Having said that, I would like to ask you a question, with regard to what you say at the top of page 3, which reads as follows:

In the postwar period, the chartered banks have shown increasing interest in developing term-lending business with small and medium-sized concerns who find it impracticable to go to the capital market.

This is the group I have in mind when I ask this question: do you consider, Mr. Gibson, that the increase in the ceiling rate or its entire removal would be a beneficial development from the point of view of contributing to the expansion of small businesses?

Mr. GIBSON: I do indeed, sir. I think this is in my view one of the principal reasons for removing the ceiling. It makes bank lending potentially more available to the types of business enterprise in the economy which do not have many alternative means of financing. Where there are alternatives they are fairly expensive. I think this is very important. I think the banks' main job is increasingly becoming a job of financing the smaller business units in the country and individuals in the country and somewhat less, the job of financing the big corporations who have many alternatives open to them. They have the money market. They can go abroad. They have the capital market, and so on. It

seems to me very important that bank activities and energies ought to be directed in this way and so long as you have the kind of ceiling you have there seems to me to be a very small chance of it.

Mr. FLEMMING: That is what I had in mind. Further down on page 3 you mention the operations of the Industrial Development Bank. I believe the Industrial Development Bank rate is now up to about  $8\frac{1}{2}$  per cent, at least I am informed it is.

Mr. GIBSON: I think sir, it is  $7\frac{1}{2}$  and it may be higher in some cases. I hope somebody will correct me if that is wrong. There are higher rates than  $7\frac{1}{2}$  I think that is the minimum.

Mr. FLEMMING: That is the information I have. I have no way of verifying it, obviously. But, I am wondering if it is part of your submission that in the competitive activity of the chartered banks, and we have to acknowledge that part of their competition is the Industrial Development Bank, the very thing that is suggested in the act presently under study would enable them to compete again in the term loaning field with a bank similar to the Industrial Development Bank?

Mr. GIBSON: Yes, Mr. Flemming; I think this is true. But I do think the area to be covered here is very, very large. I think the Industrial Development Bank, even if the banks gradually get into this more and more, as I hope they will, and I think they would if the limitation was removed, would have lots of room. I think there would be lots of room for everybody.

Mr. FLEMMING: I think it is a very fine development for them to all be in it and I think it is a great thing for them all to have practically equal rights in that field. That was really the reason for the question. Now, coming to the matter of tight money, which we in the east are very familiar with; I guess it is not confined to the east either. Do you think that over-all taking all facts into consideration, the raising of the interest rates would have the effect even without a lessening of the tight money situation of making money more readily available. I am again speaking of small businesses.

Mr. GIBSON: Even under circumstances of tightness as much as the present?

Mr. FLEMMING: That is right.

Mr. GIBSON: I think my answer to this would have to be yes, but I do not think you would notice much difference because money is very tight now. Of course, if you do free the interest rate it will not be quite as tight but it will still be very tight. I do not really think you would notice much difference under existing conditions. Existing conditions will not continue forever.

Mr. FLEMMING: Do you think the suggested increase in the ceiling rate will result in money becoming available over-all and again, taking the matter in general terms, that it would become available from a combination of all sources for longer term financing and for operating financing and all the rest, but on the average would it result in an increase in the rate of interest which the public in general would pay, and I speak about the public in general.

Mr. GIBSON: Removal of the ceiling?

Mr. FLEMMING: The suggestion, I believe, of an increase in the ceiling rate at the moment is based on long term bonds plus  $1\frac{3}{4}$  is it not? This really



results in an increase over the 6 per cent. This is what I make reference to at the moment which is really an increase in the ceiling rate, is it not?

Mr. GIBSON: Yes.

Mr. FLEMMING: My question is: do you think that over-all the cost of money would increase, in view of the fact that it is being made available from the banks getting into more lending fields so that over-all and to the small borrower and to the small business would the over-all charge, in your opinion, be greatly increased?

Mr. GIBSON: That is a very difficult question, sir. When you say over-all cost of money I find it difficult. I would say this, because I do not know how you make such an average, and I did say it this morning, that I think the cost of money to smaller businesses would on the average, over a period of time, be less. As I say, money is tight now and you cannot expect a rapid flow of money in this direction because money is not there to flow. But, when things become a little easier it seems to me that the two things, the cost and the availability of money to small business should improve in relation to what the situation is now. It is perfectly true that some small businesses are getting money at 6 per cent now. But, this is a fairly limited flow. It is not increasing.

Mr. FLEMMING: I have some connection with some businesses that are borrowing funds at 6 per cent. I was thinking more of the enlargement of the field that is going to enable people who are now borrowing from alternative sources to borrow from the banks and so over-all the average might not be increased to any great extent.

Mr. GIBSON: It could go down, provided that more money was available from the banks and this I think is something that would take some time in view of the current tightness of money. It should go down ultimately.

Mr. FLEMMING: Mr. Gibson, I was interested in what you said this morning about the banks having the plant, the branches, the personnel, the managers who were skilled in the question of loaning money, the basis on which it is done. Do you, following that line of questioning up a bit, think that if the banks were able to indulge in a greater degree of what you might call term loaning, in addition to taking care of their customers in so far as their regular operations are concerned, the result would likely be an improvement from the standpoint of the availability or the fact that the bank would be able to service its own customers. I can visualize a situation, in fact, I know of some, where an operating credit is vital and essential to the conduct of the business, and all of a sudden they find they have to have \$100,000 or \$150,000 for new equipment, which obviously they cannot get out of an operating loan. As the matter stands now it is quite difficult for the banks to meet that need, is it not? So, my question would be, do you consider that this would be an improvement? The changes in the Bank Act before us which we are studying would effect an improvement in that regard and the banks might say to the borrower: Yes, we will give you this and we will spread it over a period of six or eight years and you will pay us regularly for it. The rate of interest will be somewhat higher but we can take care of you. So, the fellow does not go running all over the country looking for someone else, who incidentally, has to go and make an examination of his affairs. They have to almost take a blood test before they will loan him any money; the strangers, I

mean, and sometimes even the fellows he has been dealing with will want a type. But my point is that, does this not have the effect of enabling the bank to render better service to all phases of their customers' operations, with a view to expansion probably in a great many instances.

Mr. GIBSON: I agree, Mr. Flemming; the sort of example you gave is the kind of thing I had in mind. I think a gradual increase in the banks' activities in this direction would be very healthy. You know how these things are financed now, it is a fairly high rate of interest.

Mr. FLEMMING: Oh, yes, I know; I know from experience. You used the word "incentive" in your brief and I was greatly impressed by the word "incentive". I think incentives are a great thing. They are all right in politics, too. It seems to me that when you speak of incentives you really mean that it is the increase in the interest rate that is going to be the incentive to the bank to loan more money; is that right?

Mr. GIBSON: Yes.

Mr. FLEMMING: They are going to have more profits?

Mr. GIBSON: This is correct, sir, yes.

Mr. FLEMMING: All right and Mr. Sharp is going to get half of them; is that right?

Mr. GIBSON: That is right.

Mr. FLEMMING: What is wrong with that? I see nothing particularly wrong with that. As a matter of fact I believe in profits.

Mr. GIBSON: My whole case is based on the theory that banks and other private institutions ought to respond to incentives: they ought to do things that are sensible and effective from the standpoint of using the resources of the country.

Mr. FLEMMING: I think my last question probably is along this line. You were speaking about the increase in the percentage rate of the various, what you might call, near banks as compared with banks, to the detriment of the banks. You say at the top of page six:

Needless to say, these are not trends which bankers view with equanimity.

That is quite understandable. Generally speaking, it seems to me that it would be a good thing if the banks had the same rights and privileges as do the so-called near banks. Do you agree with that?

Mr. GIBSON: Yes, I do.

Mr. FLEMMING: I cannot start a quarrel with you at all, Mr. Gibson. I do not see that I have many more questions to ask. At the middle of page 7, and I am again impressed with your comments, you say:

Why should not the backers of good ideas reap some return for their initiative? Do we want institutions to initiate, to promote and to develop new ideas and new and improved ways of doing things? If so, we should encourage such initiative, not remove the incentives.

These are your words, with which I am in very hearty agreement. I have no doubt that I will have occasion to use them in another place. Is it your opinion

that these particular questions you are asking in various places—this is a sample and I will ask you to confine your answer to this one—are the things you think we should consider as desirable in the interests of the Canadian people? Is that right?

Mr. GIBSON: Yes I do indeed. These are rather rhetorical questions.

Mr. FLEMMING: I realize they are.

Mr. GIBSON: I think the answers are obvious and I hope the other people do.

Mr. FLEMMING: I think that is all Mr. Chairman, thank you.

*(Translation)*

The VICE-CHAIRMAN: I now have on my list Mr. Latulippe. We are now dealing with interest rates.

Mr. LATULIPPE: I am happy to have an opportunity to put a few questions to Mr. Gibson in regard to interest rates and in regard to the way in which interest rates are decided upon. I have before me a report of the Bank of Canada showing that when the bank was opened in 1935 the interest rate had been stable at about 2 per cent excepting for a short period of time when there was a  $\frac{1}{2}$  of one per cent variation, between 2 and  $2\frac{1}{2}$ .

Nonetheless, between 1935 and 1955, the Canadian economy went through the depression, the war, the post-war prosperity inflation, depression, recession. Why this playing about with the interest rate of the Bank of Canada from 1935 on? Could you tell us who profited from this play in the interest rate, bringing it up to 6 per cent? If we look at the statistics from 1955 to 1965, we find the big companies, the shares on the stock exchange continually increasing as the cost of living increased and yet we had increasing unemployment and poverty. Can you explain to us how we have had a period of stability, how we were able to go through the war in the post-war period with an interest rate of  $2\frac{1}{2}$  to 3 per cent? How was it then that the rise in the interest rate began in 1955, and ever since then we have had no ceiling and there has been no stability? We have a constant disequilibrium throughout the Canadian economy. Can you tell us whether your report was based on the figures of the Bank of Canada and the variations in the interest rate?

*(English)*

Mr. GIBSON: That is a pretty big question Mr. Latulippe. I think the comparison you draw of the low bank rate during the period 1935 through 1955 when it was between 2 per cent and  $2\frac{1}{2}$  per cent—I accept your figures, they sound reasonable—was a period first of depression, the latter stages. We were beginning to recover in 1935 and we were using low interest rates as one of the devices to try and bring about a recovery. This did not just happen in Canada; it was used in the United States and Great Britain and so on. During the war we had a period of controlled interest rates and controlled economy. We were really controlling pretty much the whole works. We had limits on what people could do. We had limits on what things could be made. We had foreign exchange control, and so on and so forth.

After the war we gradually came around to the view, as a result of experience, I think, and I am expressing my own opinion, that low interest rates were not working very well. We were one of the countries that left the, let us



say, easy money approach rather late. Some of the European countries left this idea a good deal earlier than we did, not the British but some of the European countries. Finally we came around to the view that we had to let interest rates perform a rationing function between supply and demand; that this was one of the necessary governors in an economy that was not planned and where the decisions were made as a result of a variety of people's desires and wishes and hopes, business' plans and so on. This is one of the ways, the use of interest rates, the use of modern policy. It is one of the ways in which a market governs these demands and allocates them.

Most countries in the world by the late 1950's had come around to this position including the British and the Americans. Well we came around to it about roughly the same time as the Americans. The Swedes and the Australians, pretty well everybody, gave up this idea of low controlled interest rates and found it necessary, and I think this is the correct way to put it, to allow interest rates to be used as one of the governors in the system. In other words they want to have an active monetary policy, to use monetary policy as an active instrument and to do that they had to let interest rates free. That is a short reply to a very big question, sir.

(Translation)

Mr. LATULIPPE: I know the question is a very broad one, but then banking is very complex. Speculation and interest are very complex, but if despite this speculation, the interest rates of the Bank of Canada and chartered banks were at 6 per cent—and this contributed to maintaining stability and credit, at the level of popular demand and business—what would happen if we dropped these final stabilizing elements in the economy at present. Were we in an inflationary period, would we not be contributing to make inflation worse?

(English)

Mr. GIBSON: If we were to draw up the use of interest rates—in other words, if we were to pump enough additional money into the system, if the central bank were to do this, in order to make interest rates lower, we would indeed be contributing to the inflation. Indeed, it is the fact that there is an excessive demand over a good part of our economy that results in the relatively high interest rates that we have now. Again, sir, this is a world-wide condition. It is not just a Canadian condition.

(Translation)

Mr. LATULIPPE: Mr. Gibson, last week Mr. Sharp asked that we increase interest rates on housing loans to 7½ per cent. Would that rate on housing loans, not serve you as a basis? Would this be a basic rate on loans issued by banks? Would you not use this as your basis in calculating interest rates?

The VICE-CHAIRMAN: I would like to remind you, Mr. Latulippe, that Mr. Gibson is part of no financial institution at the present time and I would like you to direct your questions more particularly to the matter of interest rates generally. I do not think you should ask the witness what companies are going to do, or intend to do.

Mr. LATULIPPE: Yet he worked on these reports. The report asked that the ceiling be lifted, so in order to encourage financial institutions the Government

comes to their help by increasing the rates on housing loans and helps them through the Industrial Development Bank. The Industrial Development Bank Loans are  $8\frac{1}{2}$  per cent. They are trying to encourage industry by increasing the rate to  $8\frac{1}{2}$  per cent, but banks will say: "The Government is lending at  $8\frac{1}{2}$  per cent we will charge more than  $8\frac{1}{2}$ ." Is this contributing to the welfare of the people or does it not send the whole economy in balance?

(English)

Mr. GIBSON: Well, Mr. Latulippe, I have expressed my view here. I do not think any particular ceiling rate has much merit except the higher the ceiling the better because it gives more latitude for competition. Seven and a quarter per cent, I think, is the rate that Mr. Lambert was speaking of this morning when we applied that  $1\frac{3}{4}$  per cent to the current market conditions. This might be the effect of the bill at this time, now that you mention it but I do not see any particular relationship between what the ceiling on bank interest rates ought to be and the published rate for National Housing Act loans. They are in the same ball park, let us say; they are both interest rates, but there is no particular reason, I do not think, that they should be the same. The  $7\frac{1}{4}$  per cent National Housing Act loan is a government rate which is announced, and this is the rate people can make these loans at. This is a matter of government policy. The ceiling rate for bank lending is a different thing altogether. You are putting an upper limit on what people can charge. If that limit leaves reasonable latitude for competition in a reasonable range of rates it is not restrictive. If it does not leave that latitude it is restrictive. The difficulty is that interest rates change and any particular upper limit is not necessarily appropriate in the future.

(Translation)

Mr. LATULIPPE: Mr. Gibson, in your report, I think it is on page 18, you have based your research on a personal income of about \$120.00 a week. Do you not know that the average is only \$80.00 a week? Some heads of families are not earning \$60.00 a week, and I see your report is based on an income of \$5,900 a year.

(English)

Mr. GIBSON: I am sorry, sir. Would you give me the reference. That does not sound familiar to me.

(Translation)

Mr. LATULIPPE: I believe it is on page 18.

(English)

Mr. GIBSON: This is the average income of these households that were sampled, is it?

(Translation)

Mr. LATULIPPE: Yes.

(English)

Mr. GIBSON: This is not supposed to be the average of everybody in the economy. It is a sample of people in large cities and therefore it would be higher than the average for the whole economy. My recollection is that this sample was

for seven cities, I think, Montreal, Toronto, Vancouver, Winnipeg, maybe Halifax and Edmonton, I am not sure. But, it was the places where incomes tend to be highest. The purpose of this sample was to get an impression of how family balance sheets look; what debts, assets and so on that people had as family units. It was not to give you an actual average of the incomes of people in Canada. It is just a sample.

*(Translation)*

Mr. LATULIPPE: When you say that money is scarce, could you explain why there is scarcity of money? What do you mean by money scarcity, and why does it exist?

*(English)*

Mr. GIBSON: I can give you a very short answer to that. More people want money than there is money around. A lot of people have things they want to do with money. They want to build houses; they want to expand their businesses; they want to buy automobiles. They want to get credit to do these things. At the moment there is more demand for that kind of thing than there is money around. The Bank of Canada quite deliberately and, in my opinion, quite rightly, does not expand the basic supply of money to meet all those demands. Otherwise we would have a real inflation. They are at present exercising a certain restraint by not putting as much money in the system as the system would like to use, the current level of demand. This is why interest rates are high. People want more than is available at the present level of resources we have.

*(Translation)*

Mr. LATULIPPE: Now, money is scarce and yet everybody needs it, people want to improve their lot, thus making a contribution to the economy. Why is it so easy to find when a special emergency arises such as a declaration of war? Why does everything become financially possible once there is a declaration of war? Then there is no question of money being scarce. Money is found. So long as they have men and materials available, money is found. Now we have men and materials available but there is no money. We shed bitter tears over that. We say to the people: "Pull in your belts, old boys, go hungry, suffer through all this and then start a revolution. We cannot do any better for you; we have not got enough money." Where is the explanation of it? I would like to have a very clear explanation if possible as to why this is.

*(English)*

Mr. GIBSON: You ask very big questions. I would say first in respect of your diagnosis of the present situation that there are not many men and materials and equipment available, an excess supply of working people and materials today. There are some, but in a great many areas and in a great many skills there are shortages. There are shortages of people and we are getting fairly close over a good part of our economy to very full use of it. Sure, there are bottlenecks. There are some areas where people are not fully employed. There are some areas where there is some surplus capacity. But there is not a great deal, and it has reached the point in a lot of areas where demand is greater than the current supply. In wartime—this is a very broad question you are raising—the essential difference between a wartime situation and the situation in which we



find ourselves today is that in wartime we know what we are trying to do. It is not very nice but you have got to organize your resources to put people in the field and produce munitions and we cut everything else back.

You remember how taxes were raised and the big war loans and the controls all through the economy. The objectives were fairly clear. We were trying to divert people into the armed forces. We were trying to increase production of munitions, essential materials and the essential things for people to live with. That was it, and I must say as one who was an economist with the prices board in those days, there were a great many restrictions on what people could do. They were not allowed to build things they wanted. They were not allowed to a very large extent to buy things that they wanted. The program was all geared toward the war effort. This is a much simpler operation. You have an objective that the vast majority of the people in the community agree with, and they get together and try to do a job.

This is not the position in peacetime. You have a great variety of wants, desires, objectives on the part of different groups in the community, different people in the community. They all want to go about their business and do things their particular way. In a free society we do not say: you cannot do this, you cannot do that. You have to have some general controls. These general controls are exercised partly through monetary policy and partly through fiscal policy and partly through other facets of government policy. But, if everybody was in a position to make all their demands effective, you would just have a great inflation. Again, it is a very short answer but you are asking very big questions.

*(Translation)*

The VICE-CHAIRMAN: I would like to remind you, Mr. Latulippe, that you have had the floor for twenty minutes.

Mr. LATULIPPE: I want an opportunity to come back to it.

*(English)*

The VICE-CHAIRMAN: I will now recognize Mr. Johnston.

Mr. JOHNSTON: I have one question which arises out of one of your answers to Mr. Latulippe. It seems to me, Mr. Gibson, that in your mind there would then be no such thing as an exorbitant interest rate?

Mr. GIBSON: Oh, yes, Mr. Johnston, I am no more in favour of usury than you are or anybody else. Certainly there can be exorbitant interest rates. There are exorbitant interest rates. I think in the area which we are discussing today the degree of competition is such that you are very unlikely to get an exorbitant interest rate, exorbitant in the sense of taking an unreasonable margin. Interest rates are bound to be quite a bit higher because money costs more. The only way you can get money is to bid more for it, and banks and other people who are lending money, other financial intermediaries, are trying to borrow money from the public in order to lend it. They have to pay the going rate and it seems to me the judgment as to whether the rates they charge are exorbitant or reasonable depends on the margin and whether or not their profits are unreasonably high. I do not think there is any evidence that that is the case.

Mr. JOHNSTON: You have left out the usual justification which is risk, as well.

Mr. GIBSON: Oh, well, I agree, yes. Sure, there ought to be some gradation depending on risk.

The VICE-CHAIRMAN: Do you have some other questions, Mr. Johnston?

Mr. JOHNSTON: No, unless Mr. Gibson was prepared to venture a guess as to what time you began to consider the margin too wide, or if he would care to define an exorbitant interest rate a little more closely.

Mr. GIBSON: You have an act on the books about interest rates for small loans now. My own view, and indeed this is merely repeating what is in this report. These are not my views, these are the views that seven commissioners put forward, but I agree with them. We felt that that interest rate act could very well be expanded to go higher than \$1,500 and to cover a broader area. A general limitation to prevent usury is perfectly sensible.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would you say that has been true of chartered banks' rates, too, Mr. Gibson?

Mr. GIBSON: Certainly sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You think there should be a limitation on interest rates?

Mr. GIBSON: I do not think it is really necessary in the chartered banks. You know I lived in a bank for 34 years and I am very much impressed with the degree of competition. But, I think all the people wanting money in the economy ought to be subject to whatever is thought to be the right law about usury.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then you would suggest that we not consider taking the ceiling off and doing nothing else?

Mr. GIBSON: You already have, sir; this law,—I have forgotten what it is called—the Small Loans Act. I do not think it is realistic, myself, the way it is set up.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It should be far above \$1,500?

Mr. GIBSON: It should go over \$1,500 yes, sir. I think the half per cent between \$1,000 and \$1,500 is quite unrealistic. I think that should be changed. But, I do not see why there should not be a general law with regard to maximum interest rates that anybody charges, subject to certain obvious exceptions. Finance charges on small items with a service charge ought not to go on to what sounds like ridiculous interest rates. There ought to be some minimum amounts on that kind of thing.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would you, Mr. Gibson, suggest that this limitation should be embedded in legislation or that rather it should be exercised perhaps at the discretion of some government authority such as the Bank of Canada?

Mr. GIBSON: My reaction to that question, sir, if you are thinking in terms of maximum rates to prevent usury or exorbitant charges, is that there is a good deal of merit in having legislation. Although, I do admit it is conceivable you might have to change it.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes.

Mr. GIBSON: But we are talking about pretty high rates here. I mean, you are not talking about 6 per cent. You are talking about something pretty different so that need for change would not be as frequent.

(*Translation*)

Mr. LATULIPPE: A supplementary question. Do you feel, Mr. Gibson, that the banks do not make sufficient profits to justify or allow an increase in interest rates?

(*English*)

Mr. GIBSON: I am sorry, sir, I do not really understand your question. Would you mind repeating it?

The VICE-CHAIRMAN: He asked if the banks are not making enough profits so that there is no justification for increasing interest rates?

Mr. GIBSON: Oh, I see, yes. I do not think this is the real question, sir. The question is: does the interest rate make sense in terms of the forces in the market, in terms of allocating the resources in the economy. The banks are going to do their best to make a profit whatever the circumstances are. They are profit-oriented institutions. This is their business just like any other business. I would not judge this situation by profits. I would judge it in terms of what was the best way to allocate resources in the economy.

Mr. LEBOE: I would like to ask a supplementary question. There are many institutions in the country, Mr. Gibson, that are controlled on a percentage basis of their profits. Would you suggest that the banking system have this same control. For instance, utility companies, telephone companies, and so on, have actual limits placed on the amount of profits they can take because their rate structure has to be based in such a way that their profits do not exceed a certain amount. Would you consider this would be something we should look at in connection with the profits of the banking system, especially when they are going to reveal their inner reserves?

Mr. GIBSON: I do not think it is desirable; no, Mr. Leboe. I think you build a rigid kind of jacket here that inhibits the incentives. I think if you get the right incentives and freedom to work at them you have got a sufficiently broad financial structure in this economy to have competition look after the question of excessive profits. Again, even at that, I stick a little because you see if somebody does something very well and makes a high profit this should not be held against him. He may have made a real contribution to the economy. Anyhow, we have a very competitive kind of set up here normally. Again, I must except this immediate period of very tight money. We have American competition pushing into this economy from a variety of directions and the larger institutions, I do not think, can get very far off base. There are not very many protected pockets, let us say, that people can exploit in this country any more. There are a lot of people looking around, anxious to get in there and compete. So, I do not like the idea of some kind of percentage control. It seems to me you are going to limit the incentives and the responses of your financial institution to the demands on them.



(Translation)

Mr. LATULIPPE: A supplementary question. If you agree to the formula "Income-Expenditures-Profit" for institutions, if you want our institutions to have a good income, and make good profits after paying their expenses, nobody will disagree with you. But we should think of the people, too. We should attempt to apply the same formula for the people "Income-Expenditures-Profit". We want the people to enjoy the economy. It seems that the set-up is all wrong, from what I can see.

(English)

Mr. GIBSON: I am not advocating that the banks should be assured good profits, Mr. Latulippe. I am simply advocating that they should be free to compete. If they can make good profits under those circumstances, all right. I am not advocating they should have any assured level of profit at all. I do not believe in that.

(Translation)

Mr. LATULIPPE: We have nothing against institutions making profit. We are all for it. But we would want to get some formula to enable the people to live decently. You should have dealt with that point in your report. You speak of the "Income-Expenses-Profits" formula but you make no reference to its application to the people. You speak only of financial institutions. You forget about the people.

(English)

Mr. GIBSON: No, sir; I am sorry, I do apply the same formula to everybody. I believe in the competitive system, and in addition to that I believe one has to do something about the underprivileged in society as we are trying to do. But, I am not advocating different rules for different groups at all; I am suggesting the same rules.

(Translation)

Mr. LATULIPPE: We realize that if the economic system does not work and does not serve all the parties in the body politic. But are you not aware that if something is not operated as it should...

The VICE-CHAIRMAN: Mr. Latulippe, if you do not mind, I did allow you to put a few supplementary questions.

Mr. LATULIPPE: This is the last one.

(English)

The VICE-CHAIRMAN: Before I ask Mr. Lind to put his questions to our witness I must remind members of the Committee that as Mr. Gibson will not be available on this coming Thursday I would like to know if there is agreement that I should allow questions on the entire brief so that we will have a general idea of Mr. Gibson's views since this coming Thursday we might have some other brief before us, some other witnesses. I think we should take advantage of and benefit by the presence of Mr. Gibson here this afternoon and this evening, since he will not be here this coming Thursday. Mr. Gibson will be available to the Committee later on. I just bring that to your attention. It is up to the Committee to decide.

Mr. LAMBERT: Mr. Chairman, I object to general question because to me it just gets a helter-skelter into the record. If you want to look at what a witness has said about a certain subject you have to go through the whole blessed record to find it. If I may respectfully submit that we could continue questioning Mr. Gibson and carry on into the next item and then if he has to come back on a later occasion—I hope not—we will carry on with his brief in an orderly manner. But, I do object to this running all over the blessed shop and some of the nature of the questioning we have had in the past.

The VICE-CHAIRMAN: That is all right, then. Since I have heard some views I will now ask Mr. Lind to put his questions on the topic under discussion at present, which is interest rates.

Mr. LIND: Mr. Chairman, so I will not get out of order, first of all, are we dealing with Mr. Gibson's brief?

The VICE-CHAIRMAN: Yes.

Mr. LIND: We are dealing with the interest part of the brief?

The VICE-CHAIRMAN: Yes.

Mr. LIND: I do not know whether I want to question so much on the interest part of it, other than to ask Mr. Gibson one question. If the banks are allowed to raise the ceiling would his bank be prepared to raise the interest on deposits? Oh, he is not in the bank.

Mr. GIBSON: I was, Mr. Lind, but I am just not in a position to give you any assurance on that. Although it seems to me that increasing interest rates on both sides together has been the case for some time.

Mr. LIND: The only question I have, if we are staying on the interest portion, concerns the statement you make on page 9 which reads:

The need for a national code for banking activities is much more evident today than it was when the Commission's report was published.

I think you are referring here to the control of the over-all banking system, are you not, whether it comes under one law and one piece of legislation which would include the banks and the near banks and everything?

Mr. GIBSON: Mr. Lind, I am not specifically referring to a sort of over-all approach. This is the kind of approach that the Royal Commission report recommended, but it is not the kind of approach which the bill before you envisages. I am really just saying that the need for better regulation of banking activities, whether performed by banks or near banks, particularly those performed by near banks, is more evident now than it was when the commission report was published. We have had the Atlantic failure and various other troubles.

Mr. LIND: Of course you would not classify Atlantic as a near bank? They did not take deposits or anything, did they?

Mr. GIBSON: No, I would not. But I think that is indicative of the sort of problem. There was a trust company that had some difficulty in this picture, too, you see. It is indicative of the kind of problems the commission expressed a certain amount of concern about.

Mr. LIND: Is not the problem the quality of the credit that these institutions are forced to accept at the present time owing to the fact that the banks are entering their field pretty strongly, the consumer credit field?

Mr. GIBSON: I could agree with you, Mr. Lind, that it was due to the quality of credit but I do not know that these institutions are forced to accept such low quality credit. I think this is their decision.

Mr. LIND: Would the banks be prepared to offer this service to the public, these people who do not seem to be able to get credit. Are the banks prepared to extend their quality of credit so they will service this segment of the public?

Mr. GIBSON: I think they have, Mr. Lind, in the consumer credit, the personal lending area. I think they have very substantially extended over the last six or seven years the kind of loan they would make. I think they have gone quite a long way in this direction.

Mr. LIND: I think they have gone a long way in skimming the cream off the consumer business, if you will accept rural terminology.

Mr. GIBSON: I am not going to argue that point. They would certainly try to get as good business as they could.

Mr. LIND: I realize that. But, what I am concerned about is the segment of our public that does not have access even to consumer loans. If the banks are allowed to raise their interest rates, allowed to remove certain restrictions, will they endeavour to service this segment of the public?

Mr. GIBSON: All I can say to that, Mr. Lind, is I think that if the banks have more freedom from the restrictions to which I referred they will endeavour to service a wider area than they are servicing now. That is as far as I can go and again I have to make the qualification that you would not notice much activity until money gets a little less tight. There is not the money there to go out looking for this sort of business.

Mr. LIND: Those are all the questions I have, Mr. Chairman.

The VICE-CHAIRMAN: Thank you, Mr. Lind. As I now have no one else on my list who has asked permission to question on the interest rates, does the Committee agree that we move to the—

Mr. MONTEITH: May I just ask a very brief two or three questions? I do not suppose anybody can give me any figure on what percentage of the total cost of doing business the cost of money would be? I do not know whether there are any across the board percentages on wages. I know it would vary in different industries. I am thinking of the cost of borrowing in any average industry or any type of industry. What percentage might it bear to the total cost of doing business. Are there any figures of that nature at all?

Mr. GIBSON: You are not speaking of banks, you are speaking of businesses borrowing money?

Mr. MONTEITH: I am just talking about borrowing money whether it is a bank loan, mortgage, any industry.

Mr. GIBSON: It varies greatly from one business to another.

Mr. MONTEITH: Yes, I appreciate that.



Mr. GIBSON: In some business it is very important. I am sure there is a lot of information of this kind available but to give you a general answer I am afraid I just cannot do it.

Mr. MONTEITH: If, for argument's sake, an increase was allowed to  $7\frac{1}{4}$  per cent as the ceiling, which is approximately one sixth of the present rate, would a corresponding increase be considered in any other types of borrowing?

Mr. GIBSON: I am not quite sure—

Mr. MONTEITH: What I mean?

Mr. GIBSON: No, I am not.

Mr. MONTEITH: I do not know whether I do myself. I will try to put it a different way. If the cost of doing business with a bank, if the cost of borrowing money from the bank is increased by roughly one sixth, would the cost of borrowing money from any other source have any compensating increase? Would there be any relation between the two types of borrowing?

Mr. GIBSON: Yes, I think so. Interest rates tend to go up in the economy generally at any time; but not because money is getting—

Mr. MONTEITH: Well, then, private mortgage money might increase somewhat, too?

Mr. GIBSON: Yes, it could. Going back to your earlier question about the cost of money in business, it is usually a pretty small fraction of the total. A difference of 1 per cent in the interest rate on short money is not usually a very large factor in the company's total expenses. But it is one of a number of factors and of course as you get into the longer term interest rates and industries that borrow for very large capital facilities, the cost of money becomes very much more important.

Mr. MONTEITH: It probably seems a little theoretical, but I am wondering if there is any far-ranging increase in cost of doing business; whether any far-ranging increase in the cost of doing business might result as a consequence of raising the interest rate one sixth.

Mr. GIBSON: Well, it is a significant additional cost at a time when other costs tend to be rising.

Mr. MONTEITH: It would automatically then contribute to the increase in the cost of living because whoever pays the interest is going to pass it on just as you do an increase in wages.

Mr. GIBSON: Well, Mr. Monteith, it is another factor in cost. As I say, it is not a very large one but it is one of the cost factors.

Mr. MONTEITH: I have just one question; again, it is a sort of theoretical one. I think you were answering Mr. Latulippe a few moments ago on the economy as whole, and you said that money was tight and hard to get, and so on, and, if this were not so, there would be a more inflationary trend than there is. Did I gather that correctly? If money were not kept under control and kept from being too available there would be greater inflationary pressures than there are?

Mr. GIBSON: That is correct, yes.

Mr. MONTEITH: In those segments of the economy where there is a shortage of the product that the public wants to buy, where there is a real shortage, if

money were provided for the manufacturing of that product in greater quantities, would not competition tend to lower the cost of that product and as a consequence be anti-inflationary?

Mr. GIBSON: Yes, if you apply it to one product this is true. But, this is going on all the time. At any given time the demand for money comes from consumers, business people for short term purposes; that is, for carrying their inventories and for carrying their receivables; from householders, people who want to buy houses, and so on. And, from people who are making capital investments to expand their capacity. This is all part of the demand for money, and this process of capital expansion is going on today at a very high level. Indeed, this has been one of the factors which has made demands excessive. We have had a very great increase in the capital expenditures in the economy. Now, those capital expenditures will, as you say, contribute to more production.

Mr. LAMBERT: But it may be high cost production.

Mr. GIBSON: It may be high cost production, yes. But in any event they will contribute to more production. The point is that expenditures for capital goods, consumer goods, inventories, and so on, are all part of the demand at any given time. The capital goods portion is very substantial.

Mr. MONTEITH: If this capital goods demand is not met is this not going to create a tight situation in the actual end result; that is, the product?

Mr. GIBSON: It depends on how much it is not met, if you see what I mean. We have a very high level of capital investment now. It is the highest physical level in our history.

Mr. LAMBERT: Also the highest cost.

Mr. GIBSON: Yes, it is high cost.

Mr. LAMBERT: Therefore, it is reflected in a high cost for expanded production, in many instances.

Mr. GIBSON: Some of it will be high cost and some of it not.

Mr. MONTEITH: Maybe a somewhat higher cost—I am answering my colleague here now—might in turn eventually result in competition sufficient to bring down the cost of the product?

Mr. GIBSON: This is right; basically this is what capital investment is about. You are trying to increase your production of goods that people want and use. It does tend to keep costs down. People are looking for better ways of producing things. A very much larger expenditure on machinery sometimes produces a cheaper article; very frequently it does.

Mr. MONTEITH: I think those are all the questions I have at the moment, Mr. Chairman. I am getting into a field that is not altogether tied into interest rates.

The VICE-CHAIRMAN: Does the Committee agree that we now move to the second topic which is the 10 per cent limitation on ownership? Mr. Cameron?

Mr. MONTEITH: I thought it was cash reserves?

The VICE-CHAIRMAN: Excuse me, cash reserves.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I thought it was the 10 per cent limitation.

The VICE-CHAIRMAN: On cash reserves, I am sorry. Mr. Leboe?

Mr. LEBOE: I have just one brief question, Mr. Chairman. I would like to ask Mr. Gibson whether or not he believes that it would be through an evolutionary process in finance, without getting into the extent of too much dictation, because I gathered from one of the answers you gave previously, but would you believe the general policy of the Governor of the Bank of Canada, the banks and the Minister of Finance should be toward getting 100 per cent, if possible, ownership of Canadian banks or as close to that figure as possible?

The VICE-CHAIRMAN: We are on cash reserves, Mr. Leboe.

Mr. LEBOE: I beg your pardon?

The VICE-CHAIRMAN: We are on cash reserves.

Mr. LEBOE: Oh, yes, I beg your pardon. It was the question I had in my mind because of what you said previously. I will pass for the time being until we reach that part.

*(Translation)*

Mr. CLERMONT: Mr. Gibson, it would appear to me, according to your brief, that the proposals incorporated in Bill C-222 with regard to the cash reserves would make it possible to allow more money being made available to chartered banks or other institutions in order to lend money to the public.

*(English)*

Mr. GIBSON: I would not go that far, Mr. Clermont. It will put the chartered banks, in my opinion, in a better position to compete for savings, term money, because they will be required to keep a lower cash reserve against savings deposits, and because also they will be permitted, within limits, to borrow money against unsecured debentures against which no cash reserves will be required. This will improve their ability to compete for savings and term deposits, term money, and this, of course, is the source from which some of their ability to expand the type of loans we have been talking about should come.

*(Translation)*

Mr. CLERMONT: In your brief, you appear to object to the legal restrictions which it is sought to establish here with regard to secondary reserves. When the Governor of the Bank of Canada gave evidence here, he answered a question of mine. I had asked him if he was satisfied that under Bill C-222 he could exercise proper monetary control. He answered yes, with this proposed legislation, though not with the present Bank Act.

*(English)*

Mr. GIBSON: I am not sure there is not some misunderstanding. I do not think I said anything about secondary reserves in my brief. I am quite willing to comment on it, if you wish. I talk about cash reserves. I do not think I made any reference to secondary reserves. I am quite willing to comment on it, sir.

Mr. CLERMONT: All right.

Mr. GIBSON: Again, I must associate myself with what was said in part of the Royal Commission Report on Banking and Finance. I agree with it. I



do not really think secondary reserves are necessary; that is, secondary reserve requirements on the part of the Bank of Canada. Obviously, banks have to have liquid reserves but I do not think the secondary reserve requirements for the Bank of Canada are really necessary. The Bank of Canada can influence the state of credit conditions, I would think, very effectively, through influencing the cash position of the banks, through the way it influences this cash position; that is, operations in the security markets and also through its operations in the security markets in connection with management. I, frankly, am a little puzzled as to why this additional power is necessary. I know it is fashionable in the world today. Many other central banks have this power. I do not regard this as a major issue but if you ask me what I think of it, I wonder if it is really needed.

Mr. LEBOE: May I ask a supplementary question if you do not mind, Mr. Clermont?

Mr. CLERMONT: Not at all.

Mr. LEBOE: In the banking business did you not as a banker—I do not think this is an embarrassing question—when it came to security, take in confidence material, things that you did not really have any real legal attachment to, such as a title for land or some other document which was a matter of just showing confidence as far as the individual borrower was concerned? I know that they take that from me quite a lot of times. It is nothing they can legally attach but they like to know I am willing to put it on the desk. Is not this cash reserve possibly in the same light as far as the Governor of the Bank of Canada is concerned?

Mr. GIBSON: I do not think I will comment on that question.

Mr. LEBOE: Not the cash reserves, I mean the secondary reserves.

Mr. GIBSON: The secondary reserves.

(Translation)

Mr. CLERMONT: Mr. Chairman, when you speak of cash reserves, do you include in this subject the disclosure of these reserves or is it another topic? Your brief does not discuss the reserves.

The VICE-CHAIRMAN: I think this should be another subject entirely because this might come under the general questions which we will be able to put to Mr. Gibson at the end.

(English)

Are there any other members who wish to ask questions regarding the cash reserves? Then we will move on to the next topic which is the 10 per cent limitation on ownership. I will recognize Mr. Cameron.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I have just one small question, Mr. Gibson. I notice this morning you suggested that in your view the 10 per cent limitation on any single shareholder's holdings was a sufficient guarantee against foreign control of one of our banks, and that you did not see any need for the 25 per cent limitation on foreign holdings.

Mr. GIBSON: I might slightly correct that, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Did I get it wrong?

Mr. GIBSON: I did not say—I hope I did not—that the 10 per cent was necessarily absolutely satisfactory. I said I would prefer if we just did not allow foreign banks to hold shares in Canadian banks as was recommended in this report.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): At all?

Mr. GIBSON: But I said that the 10 per cent certainly would go a long way toward meeting the problem of concentration here.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It occurred to me that it might very well be, if you did not have the 25 per cent limitation that you would have the possibility of several purchases of stock up to the 10 per cent limit who, between them, would be in a position to control the Canadian bank; that is, if you did not have that limitation.

Mr. GIBSON: This is conceivable. I do not think it is very likely.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No, it may not be likely.

Mr. GIBSON: It is certainly not impossible.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You would be in favour prohibiting foreign ownership of bank stock in Canada?

Mr. GIBSON: Oh, I think this is what we are concerned about. I think our problem is that we are worried about concentration of ownership in the foreign areas as well as domestic. We really are not very happy about having large foreign banks, particularly big American banks, who happen to be on this continent, and we are concentrated a bit here, owning Canadian banks. That is a separate question altogether; but, I am talking about what future policy ought to be.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Thank you that is all I had to ask.

Mr. CLERMONT: Is his question on the 10 per cent Canadian banks may hold in a Canadian company or a non-resident company or is the percentage on foreign banks in Canada, and so on?

The VICE-CHAIRMAN: No, it is for all the banks on our side.

Mr. CLERMONT: I thought it was the 10 per cent—there are two 10 per cents. There is the 10 per cent that Canadian banks—

(*Translation*)

The VICE-CHAIRMAN: You can put your question on the 10 per cent ownership with these banks we have here or foreign banks.

(*English*)

Mr. ADDISON: Mr. Gibson, as a member of the Royal Commission which was set up by a former government which I give them full marks for, I congratulate you on your commission and your promptness in reporting. I wish some of this would rub over onto the Carter Commission. We would like to see its report a little sooner.

The Canadian Bankers' Association made no mention of foreign control of Canada banks in their brief. I gathered this morning that you agree that the 10

per cent factor we are talking about in the Bank Act which is upped to 25 per cent, was discriminatory. In your opinion, would the 10 per cent clause sufficiently restrict foreign banks from gaining control over Canadian banks.

Mr. GIBSON: I would think so. Mr. Cameron really asked a very similar question when he said two or three people might get together and thus control a Canadian bank. This is conceivable. Of course, the bill as I read it, says if any people are associated together that they be counted as one person, but then I assume you are assuming that they would not be associated legally in any case.

Mr. ADDISON: Yes.

Mr. GIBSON: I would think that generally that ought to prevent control although it is conceivable that some way might be found to get around it.

Mr. ADDISON: Do you have any other suggestions that the one proposed in the bill to limit the size, say, of a wholly owned subsidiary of a bank in Canada?

Mr. GIBSON: As I said this morning, I would hope if we wanted to limit the size of banks in Canada that we would do it in a way that was not discriminatory. In other words, that we figure out some formula that applied to all the banks and that required them all to come to the government at certain times to get permission to expand their capital, or whatever it was. I have not thought this out. Frankly, I am expressing a rather negative view here. I am not very happy about what is being done but I do not have any wonderful formula that provides a good answer to this.

Mr. ADDISON: I think we all realize this is rather a ticklish area we are in. I think a man of your experience and in your unique position of being now a professor, I assume, perhaps could give an unbiased view.

Mr. GIBSON: I am trying.

Mr. ADDISON: You suggested this morning and also in your brief that the shares of a bank held outside of Canada, provided they were widely distributed, would not affect the policy of a Canadian bank.

Mr. GIBSON: Yes, I did.

Mr. ADDISON: That would fall into the category, I suppose, then, of a 10 per cent share ownership of a foreign bank in a Canadian bank provided the other remaining 90 per cent were widely distributed in any country.

Mr. GIBSON: Yes. Naturally I am not assuming that most of the stock in Canadian banks would be held outside of Canada. Even if you do not have a 25 per cent limitation the fact is that most of the Canadians are predominantly controlled in Canada. At least, their shares are predominantly held in Canada as well as being controlled in Canada. I would not expect this situation to change a great deal.

There are certain incentives which tend to help or persuade Canadians to hold high quality stocks. We have the 20 per cent income tax rebate on dividends from Canadian stocks and this is an advantage to the Canadian holder of a bank stock or any other equity he gets where a foreign holder does not get it. So, there is a pretty fair incentive there to persuade Canadians to go on holding bank stocks. What I said this morning was that I could not really see any essential difference in the sort of country that Canada might be if some of the sharehold-



ers happen to live in cities in the United States or Britain or France as well as in cities in Canada, provided they did not control the banks.

Mr. ADDISON: You feel then, for example, the Mercantile Bank should perhaps take advantage of the provisions in this bill whereby they can split their capital stock—I think it is ten for one, twenty, is it—and say make 90 per cent of their shares available regardless of residence, in so far as protecting the Canadian banking system is concerned in which I think we are interested.

Mr. GIBSON: That is a pretty difficult question. I have not really expressed any views on what they ought to do. I do not like this clause 75(2)(g); I think it is discriminatory. I think if we want to control expansion of bank capital we should do it in a non-discriminatory way.

Mr. ADDISON: Since we have established some form of policy—whether it is the right or wrong policy—with regard to our insurance companies, trust companies, mortgage and lending institutions, our newspapers and magazines, our TV and our radio, which all require a degree of Canadian ownership, do you feel that the Mercantile Bank, which is a branch bank operation as against an agency bank and which is now owned 100 per cent by a foreign bank, should make available say 75 per cent of its capital stock to Canadians?

Mr. GIBSON: I certainly would not object if they wanted to do that, but I really do not have a view on what they ought to do at this particular stage of the game. I think that would be very nice if they decided to do that.

Mr. ADDISON: The reason for the concern, obviously, is the reciprocity which you are referring to in the Javits' proposals which supposedly are primarily aimed at the balance of payments. We really are not talking about the same thing here. We are talking about a situation whereby large foreign banks could control the banking system in Canada. I do not believe we will ever be in the position to have our banking system or banks control Americans in their system.

My last question to you concerns the statement in your brief:

—appears to prevent non-residents from starting a bank in Canada.

I find this hard to accept; even though a bank, for example, has only 25 per cent, if that is the figure, or 15 per cent, it is still, I would think, very worth while, in order to promote its service, to promote its business internationally, to have an interest. If the stock is widely controlled I think we all agree that the foreign bank in effect then will control the policy of the bank if the officers of the bank are in sympathy with the bank which holds 10 per cent or 15 per cent. Would you agree with that?

Mr. GIBSON: This could be, Mr. Addison.

Mr. ADDISON: So 10 per cent, perhaps, would do the same as 25 per cent?

Mr. GIBSON: It is conceivable if there were not any other substantial holders. If you had no other substantial holders and someone holds 10 per cent, a company, this is a very important degree of say. But, I am not sure that we quite understand each other because I was taking perhaps too legalistic a view in my brief. This is, perhaps, because some of our friends in the states take a rather legalistic view of this question of discrimination at times. It seems to me when you say that foreigners cannot hold more than 25 per cent of the stock in a bank; that is, from now on in a Canadian bank, and that no one person can hold more

than 10 per cent, well we have agreed that is not discriminatory. At least I think we have agreed. But, if you say that nobody can own more than 25 per cent it makes it perhaps not absolutely impossible for a foreign group to start a bank in Canada, but it makes it very difficult. A group of businessmen would find it very, very difficult to get together and just organize a bank abroad when they were only going to distribute abroad 25 per cent of the shares. I agree this is a rather legalistic approach. It does, when you have this kind of thing on the books, look as though foreigners could not start banks in Canada. Sometimes it is a sort of legal position but it is significant. There are other places in the world where there is nothing on the books that says you cannot start a bank but it does not follow that you can start a bank.

Mr. ADDISON: Our policy is pretty well established here. We encourage Canadian participation, let us say, in our utilities, insurance companies, banks, TV, radio, newspapers, and so on, to protect our Canadian image.

Mr. GIBSON: But you see you seem to have completely closed the door here. In the past it was not easy for a foreign group to start a bank in Canada but two that I can think of did, two groups from outside the country. And, they have to run the whole gamut. They have to go through parliament to do this, so the government has control over the process. Now, you are in effect saying that they cannot do that, by putting the 25 per cent clause in there. I just wonder if this is necessary, because this thing is within the control of parliament anyway so long as banks have to go to parliament to get a charter.

The VICE-CHAIRMAN: Mr. Addison, do you have some other questions? Mr. Leboe?

Mr. LEBOE: I just have one question. The other question I asked you before has been answered through your replies to Mr. Cameron and also to Mr. Addison, but I have this other question. Sir, when the Bank of British Columbia was originally set to come before Parliament, the Province of British Columbia wanted 10 per cent ownership. I may be wrong but if I follow your thinking you would have no fears at all of the provincial governments having 10 per cent ownership in a bank. Is that right?

Mr. GIBSON: No, I did not say that.

Mr. LEBOE: No, but from what you were saying about the United States and foreigners coming in, you were indicating—

Mr. GIBSON: Quite frankly, I do not like the idea of governments owning portions of banks. This is my own personal view.

Mr. LEBOE: In other words, you were saying that you would prefer, shall we say, American interests coming in and setting up a bank rather than having any provincial government owning even a portion of a bank, whether it be 5 per cent or 10 per cent or less, 2 per cent or whatever it might be. Is that right?

Mr. GIBSON: No, it is not. I do not prefer American interests coming in and establishing banks. Even more so I do not prefer having American banks take over Canadian banks. I would not want to see an American government have an interest in a Canadian bank. I would want that even less than a Canadian government interest. It seems to me there is a lot of merit in having a private banking system. It is more likely, over a long period of time, that a private banking system will respond to market forces. A government has different motivations. It

has social objectives; it has political objectives and so on and so forth. I think there is a great deal to be said for having your banking system respond to economic forces, market forces. I think it will do a good job in allocating resources.

Mr. LEBOE: I think I agree with you but I was wondering if we were not really on a witch-hunt though when you come down to such a small percentage as was proposed by the B.C. Bank of 10 per cent ownership by a provincial government and when we have, in effect, banks and other institutions, for instance, the treasury branches, which are doing a banking business in the province of Alberta. They do a fairly substantial banking business and this is a government controlled proposition and it has been in operation for how many years? Is it about 30 years?

Mr. GIBSON: Since the mid-thirties, I should think, something of that kind, yes.

Mr. LEBOE: If it does not prove to me in this connection, with the Quebec Savings banks and so on, that there is any need for the fear—I am not saying that I was altogether in favour of any large portion of a government interest in any bank—I am wondering if, in your mind, there was not a little bit of witch-hunting?

Mr. GILBERT: Is Mr. Leboe assuming that the Quebec Savings Bank is government controlled?

Mr. LEBOE: No, I was not assuming that.

Mr. GILBERT: Which bank is it then that you are referring to?

Mr. LEBOE: There are certain influences—if I was to get into that it would take some time—which you know of as well as I do in connection with the Quebec Savings Banks.

The VICE-CHAIRMAN: I should refer you, Mr. Leboe, to clause 53 of the proposed legislation.

Mr. LEBOE: I have it marked down here. That is all right. I was just wondering whether or not as an ex-banker, now completely removed from the banking business, perhaps we could get more of an objective answer from the witness than possibly we would from somebody that has actually got his finger in the pie.

Mr. GIBSON: Mr. Leboe, I think I would have to, as an objective bystander, say that I think it is better if governments do not get into banking, period.

Mr. LEBOE: I accept that.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Gibson, tell me if you would have the same objections toward a situation in which governments and government agencies were, perhaps, the principal depositors in a bank. Would you as a banker turn down a government account?

Mr. GIBSON: Heavens, no.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Even though it might constitute a considerable leverage of power?



Mr. GIBSON: Governments have to bank somewhere. I think it is better they should bank with private banks than set up their own bank.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Even though the size of their deposits might in effect—

Mr. GIBSON: Even though they are important.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Very important in control of the bank's operations, perhaps.

Mr. GIBSON: Well, not so important as if they controlled the banks.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No? I would have thought the threat of withdrawal might be very powerful.

The VICE-CHAIRMAN: I have on my list—Mr. Latulippe, you have a supplementary question?

(*Translation*)

Mr. LATULIPPE: A moment ago, you were saying that new banks might establish themselves in Canada, thus bringing about competition, such competition providing advantages to the citizens of this country. Could Mr. Gibson tell us why, in the past, we have had bank mergers, which was supposed to be a good thing, and now, we say the exact opposite. We say that we need new banks. If new banks are put under the same conditions, under the same rules, of what advantage will this be to the people of this country?

(*English*)

Mr. GIBSON: Well, Mr. Latulippe, we have, of course, had mergers of chartered banks in the past, with the approval of the government—the Treasury Board, I guess it is. I do not know if the number of banks is at a historically low level but it must be awfully close to one if it is not at the moment. I think what has happened is that rather than seeing a lot of new banks appear there have been a lot of near banks moving into banking. There have been trust companies growing rapidly and increasing their banking functions. Loan companies are doing this. The Caisse Populaire in Quebec are really savings banks. They have grown very greatly. Credit unions have grown greatly. So there has been a development, let us say, of specialized financial institutions, many of them of a savings bank character, outside the formal banking system, but they are nevertheless performing banking functions and this was really one of the principal problems to which our commission addressed itself. I think that is really the answer. There has not been an increase in the number of chartered banks but there has been an increase in banking competition and of a very substantial order.

(*Translation*)

Mr. LATULIPPE: Mr. Chairman, this is my last question. If Caisses Populaires or near-banks have money supplies which do not enter into the general money supply, this could not hurt the chartered banks because it is not their money.

(English)

Mr. GIBSON: Sir, I did not argue that it hurt the chartered banks. Maybe competition is good for the chartered banks. I have never argued anything here except that the chartered banks should not be restricted. I do not think the Caisse Populaire hurt the chartered banks. I think they do a very good job indeed.

The VICE-CHAIRMAN: Now I will recognize Mr. Flemming and Mr. Gilbert afterwards.

Mr. FLEMMING: Mr. Chairman, I only have one question arising out of Mr. Addison's question. Mr. Gibson, to be specific, you do not favour the inclusion of clause 53 which has to do with foreigners, or non-residents starting a bank in Canada. At the top of page 8 of your brief you state:

We should not close the door completely on non-residents wishing to incorporate banks, nor should we bluntly refuse representation of foreign banks in this country. This is out of keeping with the main stream of Canadian policy and against our basic interests.

So I assume that you feel that clause 53 is undesirable.

Mr. GIBSON: Well, the 25 per cent limit, yes. I think this does, in effect, say that a foreign group cannot start a bank in Canada. This is the question of discrimination again.

Mr. GILBERT: Mr. Chairman, I direct my question to the provision ordering the banks to divest themselves of more than 10 per cent interest in other companies. You stated this morning two main reasons. One had to do with the retroactive effect, and you mentioned RoyNat and the Mortgage Insurance Company of Canada and, secondly, the restriction on the initiative of the bank with regard to going into other fields of lending. On those two grounds, you first said that the Royal Commission put forth the principle that they wanted to limit the holding of interests of banks in other companies, and I imagine the reason for that was they did not want to have centralized power. Then you went to the second position that they made the recommendation that application should be placed before the Treasury Board which should be empowered to inquire into financial institutions and if perchance it was against the public interest—if it put the competition in jeopardy—it should not be allowed. I have wrapped up a lot of information into this but my first question is: what criteria would a Treasury Board use in determining whether banks should be empowered to invest more than the 10 per cent or whatever per cent they desired.

Mr. GIBSON: First, in answer to your question, I suggested one set of criteria. They were, when a bank in combination with some other company wanted to bring about some innovation which was useful and, indeed, our commission said we thought where these innovations were useful that the approval of the Treasury Board might come almost automatically, provided that the bank did not control the project, provided that control was divided amongst a group. I can think of a lot of other circumstances of possible criteria. You might have a situation where one of the parties was rather weak and it was desirable that it be amalgamated or controlled by a stronger partner. It is conceivable that you might permit a Canadian financial institution to own more than 10 per cent of a company than another financial institution if you thought the alternative was

that it might be bought abroad. Thinking, perhaps, of institutions other than banks the Royal Commission suggested, for example, that where institutions were small that it could not really see any objection to amalgamations. Indeed, they suggested, perhaps, that the government should not take a part if the capital did not come up to a certain minimum figure. I think there are a lot of possible circumstances. We mentioned quite a few of them in our report.

I would just like to correct an impression I may have left this morning. You did summarize what I said in a very short compass. It did not quite come out in a way that made me happy. The other point I made was that I did not think it was good to make retroactive the undoing of relationships, of contractual relationships, which have developed in many directions unless there was a very good reason for it. That was the other thing on which I expressed a very definite view. I did not think a good reason had been advanced. My own impression—and I suppose I could be accused of bias because I had been with a bank which has an interest in a trust company—is that the competition even between the trust companies and the banks increased substantially during this process in which some banks did acquire interests in trust companies. I think it is very hard to demonstrate that competition has suffered as a result of this process.

Now, you ask, how can the Treasury Board judge these things? Well, they are difficult things to judge. I think you have to set able people to work to write reports on these areas, to do some real digging and try to see what the effects seem to have been. It is very hard to judge this just by a general look. Somebody has to dig in and hire some university economists to have a look at it perhaps, and see what they come up with. This is something I think in our society people have to keep looking at. If you believe in a competitive economy you have to be concerned with concentration. You have to keep looking at this process and satisfying yourself that concentration is not impeding competition; that it is not lessening competition, or restricting it.

Mr. GILBERT: May we assume that the concentration that was going on was not restricting competition?

Mr. GIBSON: I do not think there is any evidence to support the view that it was restricting competition. Indeed, some of the motivations of people that develop such connections were to help them to compete more. But, this is something you have to look at pretty seriously and form a view on. My own judgment, from what I have seen of it, is that competition has been more severe, and, again, up until a year or so ago, in the four or five years preceding the middle of 1965, than it has been any time that I have known, between banks and other financial institutions.

Mr. GILBERT: One other remark you made, Mr. Gibson, was that—and correct me if I am wrong because I made sketchy notes—the Royal Commission thought it would be permissible, provided there was less than a controlling interest in the institution. Now, would that not be difficult if you had say two banks and three trust companies?

Mr. GIBSON: Well, actually, the examples before us at the time were RoyNat, in which there are I think a couple of banks and a couple of trust companies.

Mr. GILBERT: Yes, that is correct.



Mr. GIBSON: And the Mortgage Insurance Company of Canada in which an industrial company, a bank and an investment dealing company had an interest. So in both these cases, you see, there was no individual bank that had a controlling interest. This is the sort of context in which the commission was thinking. These things were new at the time and they seemed sensible and helpful to the community and that is the context. There might be other situations arise that you might have to take a fresh look at.

Mr. GILBERT: That is all, Mr. Chairman.

The VICE-CHAIRMAN: I think the Committee should adjourn until 8 p.m.

Mr. LEBOE: I was wondering, Mr. Chairman, as I have no further questions of this witness, if anybody else has?

The VICE-CHAIRMAN: I think Mr. Lambert and some other members told me they wanted to ask questions at 8 o'clock tonight. So we will continue the hearing with Mr. Gibson this evening.

(Translation)

Mr. CLERMONT: You have my name on the list, Mr. Chairman?

The VICE-CHAIRMAN: Yes.

#### EVENING SITTING

The CHAIRMAN: Gentlemen, I think we should resume our session which was adjourned from 6 o'clock. I am informed that Mr. Gilbert had just about completed his questioning when we recessed. I understand he has one or two other questions, so I will give him the floor right now.

Mr. GILBERT: Mr. Chairman, I would like to ask Mr. Gibson—it is really an informational question—how the Canadian banks operate in cities like New York; under what rules do they operate and what restrictions, if any, are imposed upon them? In other words, can they take deposits and make loans in New York?

Mr. GIBSON: Mr. Gilbert, this, again, is a big question. As far as the latter part of it is concerned, they are not permitted to take deposits from local companies. They can take deposits from international concerns. They can make loans. The main restriction is on their right to take deposits. This is not the whole story but, I think, this is the main point. If you want this developed, I think you should ask one of the bankers who is better informed on it than I am.

The CHAIRMAN: Yes, I think we will be inviting some of our friends from the Bankers Association back, in due course, to give us some further information on this very interesting topic.

Mr. GILBERT: I think that is all, Mr. Chairman, thank you.

The CHAIRMAN: I think perhaps I might ask Mr. Gibson something. I do not know if this has been dealt with. If you look at page 5 of your brief, I note your comments about the percentage of assets that the chartered banks seem to have come to hold since 1945 and you refer to the assets of the main financial

institutions. I presume you include in that the pension funds of insurance companies and so on?

Mr. GIBSON: Yes, Mr. Chairman.

The CHAIRMAN: If you apply the definition of banking which is recommended by the Porter Commission to the financial institutions, and you put aside the groups which would be covered by that definition, could you estimate what percentage of assets or possibly deposits the banks would have? In other words, this definition would obviously take out the—

Mr. GIBSON: Yes, it is very much higher. I cannot give you an up to date figure on that; it would be 75 percent or perhaps more.

The CHAIRMAN: Seventy-five per cent. Would you agree that, perhaps, from a statistical point of view it is interesting to look at the total asset holdings of financial institutions as a practical matter for those interested in the study of the system involving those operating a financial intermediary, including the pension funds. The insurance companies are not that useful because although they accumulate finances, they have come into existence, to some extent, for specialized purposes which nobody would suggest that banks are interested in trying to match. The bank is not trying to provide somebody with a pension after he retires; they are not intending to try and provide his estate with a sizeable fund if he passes away.

Mr. GIBSON: No, this is true, although the competition has widened quite a bit, banks are interested in term deposits. The bill before you proposes that they be allowed to issue unsecured debentures up to a certain amount. I would say that there was some competition between the longer term institutions and the shorter term institutions. The trust companies, for example, are sort of in the middle, you see; they do both these things to quite a large extent.

The CHAIRMAN: But you would agree if you just looked at the institutions to which you could apply the proposals of the Porter Commission as to the definition of banking, the banks really are in quite a dominant position as far as assets are concerned.

Mr. GIBSON: They are much the largest of that group, very much the largest, yes.

The CHAIRMAN: Of course, I should inquire whether there are other names after Mr. Gilbert who would like to ask questions.

Mr. CLERMONT: Mr. Chairman, I have given my name to the Vice-Chairman.

The CHAIRMAN: My apologies. Perhaps, I could ask the advice of the clerk.

Mr. CLERMONT: We were discussing, when we adjourned at 6 o'clock, the two restrictions, the 10 per cent and the restrictions on foreign capital investment in corporations in Canada.

The CHAIRMAN: I understand that the way the discussion evolved, there had been some linking of the 10 per cent subject with the other clauses about foreign ownership.

Mr. CLERMONT: Yes.

The CHAIRMAN: Perhaps, Mr. Clermont, I should recognize you and then Mr. Lambert.

*(Translation)*

Mr. CLERMONT: Mr. Chairman, in his brief, Mr. Gibson seems to take some objection to section 53, 1) and 75, 2g) which specifies: "exceeding twenty-five times its authorized capital stock if more than twenty-five per cent of its issued shares are held by any one resident or non-resident shareholder and his associates." and, further on—

"if, when the total number of shares of the capital stock of the bank held by non-residents is twenty-five per cent or less of the total number of the issued and outstanding shares of such stock—

Mr. Gibson, you do not seem to have any objection to any American bank asking the Parliament of Canada to obtain a charter in order to carry out banking business in Canada. But you do seem to object to Canadian banks being controlled by American banks. Do you have any objections to American banks, or a group of non-residents asking the Canadian Parliament for authority to operate a banking business in Canada?

*(English)*

The CHAIRMAN: Mr. Gibson, do you have any comments you would like to make?

Mr. GIBSON: Mr. Clermont, the position I took was that I did not think that American banks, and I said foreign banks, not American banks, should be permitted to control Canadian banks. I did say that with respect to one of these started banks, it seemed to me, additionally discriminatory. I think we have to be discriminatory to some degree here if we do not want American banks to get larger interests in Canadian banks. I think this is something which one has to face up to, but I did say that it seemed to me that the 25 per cent requirement of maximum foreign ownership made it almost impracticable or almost impossible for a group of people from abroad to start a bank in Canada. I would argue that banks abroad should not be permitted to start banks in Canada.

*(Translation)*

Mr. CLERMONT: At the bottom of page 8 of the French version, you speak of American banks. Let us give an example, let us speak of the Chase National Bank or the Bank of America. Let us assume that these banks were to ask the Canadian government for authority to set up a bank in Canada. Do you not think that it might complicate the work of the Bank of Canada with respect to the monetary control, their source of income being practically unlimited?

*(English)*

Mr. GIBSON: It might, in time, perhaps, Mr. Clermont, you misunderstand me. I said that I did not think that foreign banks, and that includes American banks, should be allowed to establish banks in Canada or buy them. I pointed quite specifically to the problem of concentration and I said that our commission had the view that we did not want to see undue concentration of the financial system in Canada, for fear it might limit competition and that this applied to



concentration coming from abroad, too, because we live in the North American continent and New York is the great financial centre. It seemed to me that this was a problem here and that we have to face up to it.

Now, the proposed legislation agrees and will allow, as I understand it, a 10 per cent ownership by an American bank. I did not object to that; I said that the commission would have gone farther and did in its recommendations, but the 10 per cent ownership would certainly limit the process of concentration. It might prevent it altogether.

*(Translation)*

Mr. CLERMONT: I am sorry, Mr. Chairman, but I feel I should return to this point. Speaking personally, I feel it would be far more dangerous for a group of non-residents to seek to establish a bank in Canada, especially if these were American citizens. It could very well happen that an American firm, with its head office in the United States, would call upon its Canadian subsidiary to deal with this American based bank instead of dealing with a Canadian bank.

*(English)*

Mr. GIBSON: I am not quite sure that I understand your point, sir, because it seems to me that if you are assuming that the 10 per cent rule would apply—

Mr. CLERMONT: No, the 10 per cent does not come in my mind at all, Mr. Gibson. I am speaking about non-residents asking Parliament for a bank charter.

Mr. GIBSON: Yes.

Mr. CLERMONT: In your brief you do not seem to have any objection to non-residents having full control of a bank, not 10 per cent, not 25 per cent but full control.

Mr. GIBSON: No; I think it would apply to whatever the law was. The proposed recommendation here is that no one individual or corporation should have more than 10 per cent control of the bank. What I am saying is within that context.

The CHAIRMAN: Let me ask you this question; if I could, perhaps, interrupt Mr. Clermont for a moment. Perhaps you dealt with this this morning but could you explain why you felt that clause 53 would appear to prevent non-residents from starting a bank in Canada?

Mr. GIBSON: Because it says you cannot have more than 25 per cent foreign ownership in a bank.

The CHAIRMAN: Would this not permit a group of people to apply for a charter and not hold more than 25 per cent?

Mr. GIBSON: Yes, it would, if you could do that. Could you have a group of people who did not represent more than 25 per cent of the ownership start a bank? I do not really see how you could do this.

The CHAIRMAN: Am I mistaken in this or not, Mr. Elderkin, that with the two charters we have just considered in the last few months, the Bank of Western Canada and the Bank of British Columbia, initially the Treasury Board

permitted the incorporators to have more than the maximum permitted provided they divested themselves of it by a certain period?

Mr. ELDERKIN: This was the case with the Bank of Western Canada, Mr. Chairman, and this is clause 57, which gives a certain amount of overriding authority to the Treasury Board or to the Governor in Council later but only at the present time in the case of resident shareholders not of non-resident shareholders.

The CHAIRMAN: I see, but if the non-residents wish to associate themselves with Canadians they would—

Mr. ELDERKIN: Of course, Mr. Chairman, if one wants to really look at the technicalities of the thing, Parliament can always in the charter of a bank, override previous legislation.

*(Translation)*

The CHAIRMAN: I am sorry Mr. Clermont, but I felt that it might be useful to clarify that point. Have you anything else?

Mr. CLERMONT: Under 76 (1), which refers to the ten per cent controlling share, Mr. Gibson mentioned that banks have contributed to the establishment of institutions such as RoyNat. He said that they had given rise to new ideas. Now with regard to trust companies generally, Mr. Gibson, do you not feel that banks have used these trust companies to enter into an area which was prohibited to them through the provisions of their charter?

*(English)*

Mr. GIBSON: No, sir.

*(Translation)*

Mr. CLERMONT: Well, I know very well for one, that provincially, at least, a few years ago, somebody who borrowed from a chartered bank under the N.H. Act could not enjoy a discount on the interest rate, which was provided for at the time in that province, but if you borrowed from the Bank of Commerce, you did not have a discount, but if you had it from the National Trust, for instance, which at the time had a relationship with the Bank of Commerce, I believe that you could have it.

You see, there was a provincial act in the province of Quebec providing that if you had a loan from a Caisse populaire at interest rate of "X", it was possible for you to have a discount on that interest rate. So the act read, but if you borrowed under the National Housing Act, you could not have that discount. That was the thinking of the administration at the time. It was changed of course, subsequently. But if you borrowed from the banks under the N.H. Act, it was impossible to obtain that discount, whereas if you borrowed from a trust company, you could.

Since these banks had some relationship with the trust companies, did it not make it easier for them to do that, since they were not allowed to make any such loan before 1954?

*(English)*

Mr. GIBSON: Mr. Clermont, I really am not familiar with the situation which you are discussing. I take it that there was a discount arrangement which the

government of Quebec introduced and which the trust companies handled but the banks did not. Is that correct?

(Translation)

Mr. CLERMONT: That is correct, because the thing did happen in Thurso, and I remember very well that people had to borrow from the National Trust, they could not go to the Bank of Commerce.

(English)

Mr. GIBSON: I am sorry, sir, I am really not in a position to comment on it because I do not know the situation.

(Translation)

Mr. CLERMONT: But, Mr. Gibson, what I am getting at is this, I mentioned to other witnesses for instance, that the Bank of Montreal has some financial interest in the Royal Trust, the Royal Bank has some relations with the Montreal Trust, that you have shareholders in the Royal Trust who are in one bank and the Montreal Trust in another bank. Do you not believe that this relationship between these institutions made it possible for them to enjoy additional income?

(English)

Mr. GIBSON: I will not comment on your description of the interlocking arrangements. I am not altogether sure that this is thoroughly accurate, sir, if you do not mind my saying so; but nevertheless, admittedly there are such relationships and certainly this is a matter of convenience. It is helpful, presumably from the standpoint of both parties. I do not see that it is necessarily good or bad; it depends on what the results are.

(Translation)

Mr. CLERMONT: But you, Mr. Gibson, on page 7 of your brief, French version, (probably page 6 of the English version) you admit that the fact that banks have gone to the trust company business has given rise to additional competition.

(English)

Mr. GIBSON: Yes; I think it has lead to additional competition. The trust companies which banks have become associated with, particularly the more recent associations, seem to have become very competitive and active.

The CHAIRMAN: With their associate banks?

Mr. GIBSON: Competitive with their associate banks? To some degree, yes, sir. But certainly competitive and active in relation to everybody else.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Are you referring to RoyNat?

Mr. GIBSON: No; we are talking about trust company-bank associations, as I understand it, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You spoke about more recent developments and I wondered if you had in mind RoyNat.



Mr. GIBSON: No, I was thinking just of the trust company and the banks.

Mr. LAMBERT: I find a curious paradox, if I may say so, Mr. Gibson, in what you have just now said, and what was indicated in your brief with regard to the question of foreign ownership of banks in Canada. I think we all agree, and the position you have taken in your paper, is that there should not be any takeover of existing Canadian banks.

Mr. GIBSON: Right.

Mr. LAMBERT: If you are limited to that, then I would go along with you but, on the other hand, I cannot agree with your paper and I, personally, cannot agree that a group of foreign citizens with sufficient capital could not come to the parliament of Canada to obtain a charter. We did it with the Mercantile Bank; there were Dutch interests.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): They did not come before parliament.

Mr. LAMBERT: The Mercantile Bank had to, with the greatest respect—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But the takeover did not come before Parliament.

Mr. LAMBERT: But the Mercantile Bank was not a Canadian owned bank. It was a Dutch bank and I cannot see the difference and I, personally, have no, if I may say so, great worries about either the First National—they are in here, now, anyway with the Mercantile Bank but should I say, Chase National or the Bank of America or one or two of the others. If they want to come before parliament and seek a charter to operate a bank, they are going to have to compete with an already well set up system. We have not seen the Mercantile Bank, for instance, expand greatly. Yet, I find the position you have taken with regard to foreigners incorporating a bank in Canada inconsistent with your original promise about the benefits of free competition and, also, I find it somewhat a contradiction to the desire of Canadian banks to operate in the United States or abroad. If, what is good for us abroad, surely to goodness, must be good for those here. I think the government under its present proposals has embarked on a very, very dangerous adventure, as far as our chartered banks are concerned.

Mr. GIBSON: Mr. Lambert, I think you are putting forward a very real problem in this picture. This is the question of when concentration and free competition come into conflict. Lines have been drawn, so far as the domestic economy is concerned, in this bill. It is made clear that the government does not want undue concentration in the banking system in this country—further concentration of a financial system, let us say. When you look at the relations with the United States which is really the most important area we are talking about when we are thinking about concentration, some of us say, well, we are not happy about the idea of the big American banks controlling Canadian banks.

Mr. LAMBERT: I will go along with you there.

Mr. GIBSON: You will go with that; then you say,—

Mr. LAMBERT: I will go along with you there that they should not come in to take over present Canadian banks. I think, generally, that is the accepted

position all the way through the Porter Commission and is what most witnesses have said, but there I stop.

Mr. GIBSON: Then by your 10 per cent—I have to ask you—it is not my business to ask you questions—what do you mean? There is a 10 per cent clause in this bill that no individual or corporation or entity should own more than 10 per cent of a bank. How do you relate this to an American bank, let us say, asking for a charter to incorporate in Canada?

Mr. LAMBERT: If its proposed shareholders will qualify under our domestic rules, what is wrong with that?

Mr. GIBSON: But the ownership would be concentrated in one place.

Mr. LAMBERT: One country.

Mr. GIBSON: You see, this is what I am trying to say. This is why I think the 25 per cent creates a real problem. If the 25 per cent applied to all foreigners—you get a group of foreigners together who are not necessarily related. They might be able to raise 60 per cent of the funds required to start a bank and they will come and ask for a charter. But by putting the 25 per cent rule in, you tell them that, in effect, they cannot do that. I would have thought that the 10 per cent proposed rule which you have here would have prevented an American bank from coming and asking for a charter to incorporate in Canada.

Mr. LAMBERT: Yes, I would, if the bank itself were going to own the shares but that is not envisaged. Surely, that is not envisaged for individuals wishing to incorporate. At the present time, nobody but Canadians can incorporate banks in Canada under the present legislation, that is, effectively. This is what I object to and I object strenuously to this Mercantile set-up because it is discriminatory and I think it portrays a fit of pique on the part of someone. You have the controls on the capitalization; no Chase National Bank will come in here to incorporate at, say, \$200 million in order to suddenly try to take over the Canadian system. It has to do business in this country in order to be effective. I think the Canadian banks can point out that they have achieved their present position, some of them as a result of 100 years' operation. It has taken time and they are not country bumpkins when it comes to banking practices. I am not afraid of them, at all, as far as that part is concerned.

Now, as to an American or British or French interest buying in the control say a 10 per cent slice of an existing Canadian bank, I agree with you, and I think the limitation of 10 per cent is a good one since they are public corporations and effective control could be cornered, let us put it that way, with a 10 per cent interest. I found your position, if I may say so, about foreigners not being able to come in and incorporate a Canadian bank, that is Americans, paradoxical with the rest of your paper.

Mr. GIBSON: Let me put it again. As I read this bill, there is a 10 per cent clause proposed which says, in effect, that no bank, whether a new one being incorporated or a present one, is to be owned more than 10 per cent by one entity, with the exception of banks that already are, and here is one such bank. It seems to me that if you take this 10 per cent rule seriously, and I am inclined to take it quite seriously because I gather it has been applied in the thinking to the Bank of Western Canada although an exception has been made to the rule but still this means that the general rule is taken seriously, all I said to you was

that the 10 per cent item was non-discriminatory because it applies to Canadians, Americans, Englishmen, Frenchmen and everybody. I am not sure this is the best way of doing it but, in any event, thinking in terms of the question of discrimination, this is not discriminatory, I said the 25 per cent was discriminatory because it means that anybody outside the country cannot in effect, come and ask—or any group outside the country, not an individual—for a charter here because 25 per cent is not enough to come and ask for a charter, as a practical matter, I would think; so I said I thought this was discriminatory and I also said that I thought that clause 75(2)(g) was discriminatory because it applied to only one bank. I also said that this is a pretty legalistic sort of argument. I think we are talking about a pretty legalistic sort of subject. Our friends in the United States, I think, take a rather legalistic view of this question of discrimination, and we have something in our statute that almost says, that people outside cannot have anything to do with the starting of banks in this country. I think they take exception to this.

I do not want to pretend I know the answers to this; I think this is an area that, frankly, needs a lot more study. I would like to do a lot more thinking about it before I came out with some positive ideas. I think there is a lot that we do not know, that we have not found out about this story and what its possible implications of various lines of policy are. I am sorry to be rather negative about it, but that is really as far as I can go.

Mr. LAMBERT: I had the impression that maybe I had misjudged your stand by your replies to Mr. Clermont, but it seemed to me that at one point or another your answers to Mr. Clermont were quite unequivocal that you opposed foreign ownership of banks in Canada, not present banks, but all banks.

Mr. GIBSON: I am sorry to have created that impression. If I did, I did not mean to do so.

Mr. LAMBERT: That has cleared up the point as far as I am concerned

Mr. GIBSON: What I meant to say is what I have just been saying to you.

Mr. LAMBERT: Thanks very much for clearing it up.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): What distinction do you make, Mr. Gibson, between foreign interests buying into an existing Canadian bank and getting control of it and foreign interests entering the field *ab initio*, as I think my legal friend, Mr. Gilbert, would say, and setting up a bank of their own? What is the difference in your view? Suppose American interests or, for instance, suppose the Narodny Bank of Moscow decided it would like to get into the Canadian picture—

The CHAIRMAN: They are supposed to be very competitive.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I gather they are, yes, so I believe in them. It might cause us a few problems.

What is the difference in your view between foreign interests—the Narodny Bank of Moscow or the First National Bank of New York—coming in and buying up an existing bank or getting control of it and coming here and getting a charter to start up a bank in competition, because I think we will have to admit that probably in both cases they would be prepared to pump in funds to the



point where they would be a serious factor in our banking system. What is the difference?

Mr. GIBSON: One of the major differences is that if they bought a big bank it has a big operation already and a lot of influence already; but I want to ask this, I was not advocating that foreign banks be permitted to come and apply for charters to set up banks here. As I said, I think this 10 per cent proposal rules that out, and if that is discrimination, I think I would go along with that much discrimination because I think there is a problem of concentration here and you get a conflict.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Should we not be prepared to discriminate in certain circumstances?

Mr. GIBSON: I think that where we are agreed that our basic national interests are involved, that sometimes there is some discrimination involved. I do not like it but sometimes you have to make a choice.

Mr. LAMBERT: That will provoke my next question.

How loud do we scream if retaliation is taken against Canadian banks which are operating abroad?

The CHAIRMAN: Are the problems of the same proportion?

Mr. LAMBERT: It is very easy to throw stones but just make very sure you do not live in a glass house if you do so.

Mr. GIBSON: Mr. Lambert, I am more than conscious of this. I think this is a very difficult area; certainly, the Canadian banks do operate abroad and they want to be treated fairly; they do not want to be discriminated against and we are talking, particularly, here about our relationships with the United States. This is a particularly difficult problem because the United States is such a pre-dominantly important economy as far as we are concerned; our economy is so tied in with the American economy. I do not know that you could say it is quite the same thing; that it works exactly the same way. New York is the financial centre of the world. It is natural that there should be banks from all over the world in New York; it is in the interests of New York to have banks from all over the world there. I am not quite sure that you say it must work exactly the same way, the other way round.

Mr. LAMBERT: That is an arguable point; I will concede that but, on the other hand, I just cannot accept the fact that we would act in a way which would invite retaliation, and I think it is to the credit of the Canadian banks and it would assist their competitiveness; it would give them new ideas if they were able to enter into, shall we say, the American and Caribbean market, if you want to call it a market, to operate. But, on the other hand, if we are going to discriminate against the others—against other nationals—surely, we cannot complain if they were to discriminate against us. Further, you may have different ideas but I think that any foreign bank which came into Canada to start operations would have to scratch like the very dickens for a long time even to get a decent foothold and that its impact on the Canadian market would be somewhat negligible for many years to come. I may be wrong on that. Some people with far more banking experience than I have could tell me differently.

Mr. GIBSON: That is a matter of opinion, sir. I do not think I would quite go along with you but, you see, I am concerned about this question of discrimination. I do not think we should do things except in cases where we strongly feel that our basic interests are involved, which do involve discrimination. In this area, which is the area of concentration, I think that we should draw a line; the commission thought we should draw a line and you agree. It is just a matter of, before you draw this line, I do not think we should have this 25 per cent rule in regard to banks because I think it means that we are saying that a group of people from the United States or Holland or some other country who want to start a bank here in conjunction with Canadians, cannot do it. I do not see that concentration is involved in this kind of thing and I do not think we should say they cannot do it.

The CHAIRMAN: In conjunction with Canadians? Is this not what they can do?

Mr. GIBSON: Well, 25 per cent—

The CHAIRMAN: Plus other interests provided by Canadians?

Mr. GIBSON: Seventy-five per cent, yes. I do not think the people who primarily get busy and organize a bank think that 25 per cent is enough, but this is a matter of opinion.

Mr. LAFLAMME: Mr. Chairman, may I ask a supplementary question regarding discrimination? It could, maybe, apply to the 25 per cent but my question has to do with the 10 per cent. I do not think that any bank operating abroad should complain about receiving the same treatment as the other institutions in that country because the 10 per cent applies to all banks.

Mr. LAMBERT: The 10 per cent is non-discriminatory.

Mr. LAFLAMME: Yes.

Mr. LAMBERT: I think I have gone far enough. I wanted to clear up the point here. We can come back to it later.

The CHAIRMAN: I just wonder if this may also have been asked when I was at the Immigration Committee meeting but you noted, I presume, the announcement of the Minister asking us to consider the possibility of agencies of foreign banks being allowed to operate here. Now, assume for the sake of argument, that such a condition was written into our law, would that modify in any way the thinking or the proposals you put forward in your brief with regard to operations of foreign banks?

Mr. GIBSON: I have suggested, sir, that we should permit agencies. The Royal Commission on which I sat also suggested we should permit agencies. I go along with that theory.

The CHAIRMAN: You think that in view of the type of operation that the agencies of Canadian banks are presently carrying out in New York, that if, again for the sake of argument, the proposals in this act were put into law, they became law, there would necessarily flow from that some limitation in the operation of these agencies in the United States?

Mr. GIBSON: I would not like to answer that question. It is quite possible that there may be some reaction. You, presumably, have read the paper prepared

for the American Economic Committee by this professor from Columbia—I have forgotten his name—

The CHAIRMAN: Zwick.

Mr. GIBSON: Zwick, yes, and there is the Javits' bill there now which has certain possibilities of—retaliation is not the right word—changing the rules on people who do not give you the same kind of treatment. This idea is in this bill but the bill has not been passed; I do not know.

The CHAIRMAN: Does that legislation not deal as much with the United States foreign exchange problems as with anything else?

Mr. GIBSON: I would think so, yes.

Mr. LAMBERT: A sort of negative reciprocity, I think, would be a good term for it.

The CHAIRMAN: Are you finished your questions, Mr. Lambert? Your questions are so stimulating that they lead to various supplementary questions.

Mr. LAMBERT: No, I am finished. Thank you.

(Translation)

Mr. CLERMONT: Mr. Chairman, could I put a supplementary question in regard to the 25 per cent? Mr. Gibson seemed to think that the 25 per cent would not be important in regard to non-residents who wanted a charter for a Canadian bank. But in 1964, the British Columbia government asked parliament for a charter providing for a 10 per cent participation by that province. The sponsors claimed at the time that the subscribed capital of \$100 million could be easily achieved. When they came back before this committee, there was no longer any question of the 10 per cent. Instead of having \$100, they claimed they would have 30 or 50 million subscribed capital. Let us suppose that the Chase National or the Bank of America intended to subscribe 25 per cent in a Canadian bank. Would this not make the financial institutions confident that they could put up the other 75 per cent?

(English)

Mr. GIBSON: Yes; I think it would give them confidence if they could raise additional money. I do not quite get the point of your question, sir.

The CHAIRMAN: If I may say so, Mr. Clermont was, perhaps, carrying on the thought that I have that really even if the foreign interest is only 25 per cent it would not be that hard to find Canadians who would put up the other 75 per cent, and if the 25 per cent group involved the Chase National Bank or the Bank of America it might encourage some businessmen—

Mr. GIBSON: Yes, but the problem I am having with that is that you have this 10 per cent limit to start with which prevents—if you accept this proposal—the Chase National Bank or the Morgan Guarantee, or whoever it is, from putting up that additional amount, the 25 per cent.

Mr. LAMBERT: May I interject a comment. Who would be silly enough to put up \$25 million without the control in their hands?

(Translation)

Mr. CLERMONT: The government of British Columbia was ready to put up 10 per cent.



(English)

Mr. LAMBERT: They had other reasons. They were not going to control.

(Translation)

Mr. CLERMONT: No, but they were ready to put up 10 per cent.

(English)

Mr. LAMBERT: As the prestige shareholders.

The CHAIRMAN: Mr. Gibson, perhaps you can tell us from your experience what percentage of ownership would be necessary to control a banking institution if the shares were generally widely held? What would happen if you had 10 per cent or 25 per cent and the rest of the shares were fairly widely dispersed? What would be your impact?

Mr. GIBSON: It would be very substantial. If the shares were widely dispersed and you held 10 per cent even or 25 per cent, such a group would probably have a good deal to say, but you cannot make this kind of statement in a vacuum. What would the other shareholders do in these circumstances? Maybe they would get together. This is very hypothetical, sir.

The CHAIRMAN: Oh, yes, certainly.

(Translation;

Have you finished your questions?

Mr. CLERMONT: I wanted permission to put a supplementary question. One question.

(English)

The CHAIRMAN: Have we concluded our questions on this general theme? If we have, then I would invite the Committee to move on to the topic of supervision of the banking system and linked with that, of course, the proposals or suggestions with regard to deposit insurance.

I recognize Mr. Lambert.

Mr. LAMBERT: Mr. Gibson, I was interested in your approach to a definition of banking. This is something that I have found curiously lacking in the Bank Act, because it seems to me there are a number of consequences which flow from, shall we say, the commencement of banking and the whole legal definition of banking. I was wondering why the Porter Commission had—perhaps, because it found it impossible to do so and maybe you can tell us—omitted a legal definition of banking.

Mr. GIBSON: Mr. Lambert, we tried to produce a definition of what banking is—I am worried about the word “legal”; I do not know quite what you mean by that—but we did produce a definition of what we have called the banking function.

Mr. LAMBERT: There is a recent case out in Alberta involving a defence that the treasury branches were ultra vires because they were against the Bank Act. Now, this is a legal consequence which would flow from this. Look at clause 13 (1), for instance. It says: “The bank shall not commence the business of banking until it has obtained the approval of the Governor in Council thereto.”

That is on page 8 of the bill. When does it cross that magical threshold of commencing the business of banking? What activities would it have to engage in and what activities might it not engage in before someone would say, you cannot because you have not obtained the approval of the Governor in Council. This is what I call the legal definition of banking. Also, the parliament of Canada is granted the sole jurisdiction over banking by the B.N.A. Act and I think this is going to have legal consequences.

Mr. GIBSON: I should not want to take you on from a legal point of view. My background is as an economist and the definition to which we came was really an economic definition, although I think it is a common-sense definition of banking. We said the thing that distinguishes the banking function from other functions is the character of liabilities that banking institutions take on. The fact that their liabilities are liquid, are used for money; that they are close to being like money; that people use them as a means of payment, and we said that, therefore, you must, in effect, define banks in terms of the nature or the degree of liquidity. The definition must rest in the area of the degree of liquidity of their liabilities, and that the assets side is very difficult because assets vary between financial institutions but you can see this degree to which these institutions contribute to means of payment on the liability side.

We said that we did not really know where you draw the line as to how liquid a liability should be before you regard it as banking. We suggested that you draw a line of deposits payable within 100 days—you still have to draw a line somewhere. Some people would argue that banking—to go to the most extreme case on the liquid side—might be regarded only as the function of taking deposits payable on demand, current accounts. Other people say you really should take in things which are very close to the equivalent of bank deposits and go right out looking at some of the money market paper—the short term paper—but these things are very like deposits. You must draw a line somewhere. We said draw it at 100; maybe you would like to draw it in terms of something more liquid, I do not know. This is the way we thought banking ought to be defined. How this would stand up legally, I would not know. It would depend on what the courts said.

Mr. LAMBERT: I think you are getting at the same thing that I am. I would want my definition wide enough that I would be able to supervise the Canadian financial system through the definition of banking, through the Bank Act, because outside of the chartered banks, supervision of financial institutions and, may I say, the federally incorporated trust companies, is shall we say, conspicuous by its absence.

Mr. GIBSON: Federal supervision, yes.

Mr. LAMBERT: Well, any supervision

Mr. GIBSON: It varies.

Mr. LAMBERT: Meaningful supervision. This has become much more important and we realize, as the Minister of Finance said yesterday, that we now take a much more serious look at this. I would have thought that the situation had been serious long ago.

Mr. GIBSON: My own view is that this is a very serious problem. I do not think it is going to be easier to define banking by waiting. Some people think it

may; if the activities of the people who are near banks—very close to being banking—increase relative to the banks in future, then the problem in a way becomes more difficult. If they do not grow as fast as the banks in the future, the problem, perhaps, becomes somewhat less. But, there certainly is a problem here when you have a large group of activities going on in the area of banking. This is one of the things that we made no bones about in our report and the people doing these things are not regarded as doing banking in terms of law. They are not under this act but this act says, in effect, that banks are the institutions named in Schedule A; that is all. They are banks. Someone else can do something almost the same or just the same, really, but they are not a bank.

Mr. LAMBERT: I have yet to find any practical distinction between the operations, say, of the treasury branches of the province of Alberta and the branch of a chartered bank across the street, with the possible exception that the treasury branch sells hail insurance and fire insurance. Outside of that, they operate the same way, and merely because their name does not appear in Schedule A, it means that, presumably they are not under the control.

This was a point that had been developed by, I believe it was someone on behalf of the Canadian Bankers Association, that with the growth of the near banks relative to the whole of the financial system, any control action by the Bank of Canada becomes progressively more severe in its impact because it is working on a decreasing base as we go along and, therefore, to get, shall we say, the effect on the whole system, it has to press that much harder on that declining base over which it has control. Am I right in my supposition?

Mr. GIBSON: I understand your point very well indeed. I do not know whether you are right or wrong when you call it a decreasing base. It has been a decreasing base in recent years. This is perfectly correct. Whether it will be in future, I am not sure.

Mr. LAMBERT: Are there any factors to suggest, at the present time, that it should be decreasing; that their activities have reached a plateau?

Mr. GIBSON: There are some factors, yes. The banks have been competing pretty vigorously lately, and the effect of the Atlantic business, and so on, has made it more difficult for some of the newer institutions in the near banking field. I am not sure whether this tendency is still continuing. I think it would be likely to continue if the banks were subject to the kind of restrictions to which they are now subject, but if those restrictions were removed, this tendency might not continue. I would think this was desirable.

Mr. LAMBERT: I agree there is a potential problem here. I would say a real problem although I know the Governor of the Bank of Canada does not attach a very heavy weight to this problem.

If clause 76 remains as it is, which means that the banks will have to spin off a number of their holdings in affiliated operations which have made them more competitive and, perhaps, have contributed to this levelling off of the activities of the near banks, if they must now withdraw from those fields, surely, is it not natural to expect that the near banks will then move in and gradually continue their pressure and their increase in the share of the financial operations of the country?



Mr. GIBSON: I do not like the idea, as I have explained to you, of making these things retroactive and asking the banks to withdraw from this area. I am not sure that your reasoning holds. I think that the effect of the banks having closer relations in some cases with trust companies has, perhaps, stimulated the growth of the trust companies. It does not follow, in my view, that if these ties were severed, for which I do not see any good reason, but if they were severed, it does not follow, in my view, that these near banks would grow faster than they are growing now. They might not grow as fast; I am not sure.

Mr. LAMBERT: Thank you, Mr. Chairman.

Mr. LAFLAMME: Mr. Gibson, if I may ask a supplementary question, as I think it is a very important point; independently of the question of whether or not the near banks are banks or not or do the same business as banks, what are your views on how those institutions can be controlled by the Bank of Canada, if they can?

Mr. GIBSON: My view on how the near banks might be controlled by the Bank of Canada?

Mr. LAFLAMME: Yes.

Mr. GIBSON: I think this is very difficult unless you have some basis of saying that they are under federal jurisdiction. They do banking and, therefore, as banking activities are subject to federal regulations, I suppose the Bank of Canada might make arrangements with them on a voluntary basis.

Mr. MONTEITH: May I ask a supplementary question? The control of the near banks by the Bank of Canada really is not going to be effective, other than possibly on a voluntary basis, by any deposit insurance legislation.

Mr. GIBSON: I would think that was correct. I do not see that the deposit insurance proposal has anything directly to do with the Bank of Canada's relations with banks. The commission suggested that the near banks should keep cash reserves with the Bank of Canada but this is all subject to the idea that banking be defined, and that the people who are performing banking functions be subject to federal regulation. That was all part of that picture. I suppose it would be possible for the Bank of Canada to try and work out some voluntary arrangements of this kind with near banks.

Mr. MONTEITH: Mr. Chairman, this question is maybe not quite apropos, but the banks did present a case claiming that some of their deposits, at least part of their cash reserve deposits, should bear interest, should be of an interest bearing type. I would be surprised if you did not agree with this, Mr. Gibson.

Mr. GIBSON: I do not know whether I do, Mr. Monteith, or not. I do not think this is a very important question.

Mr. MONTEITH: How much might it amount to in any one bank or all the banks together? In dollars, how much might it amount to.

Mr. GIBSON: It might amount to quite a bit, but this all brings you back to the question of cash reserves. The cash reserves as proposed in this bill do not need to be as large as are proposed in the bill, but this is what is proposed, and they are in the right order now. We have high reserves for credit accounts; lower reserves for saving accounts and no reserves for long term debentures. This is right; this is the right order, but the amount of the reserves is still, certainly, in

the current accounts, larger than it need be. No bank, no institution likes carrying non-interest bearing deposits but the Bank of Canada does need, I think, to have some rules about cash reserves. I think it does, substantially, facilitate its job. It is not essential, but I think it does help a lot.

I think this question of interest is of some interest but I am not sure that it is the centre of the picture.

Mr. MONTEITH: I guess nobody likes to have idle funds.

Mr. GIBSON: No; banks would obviously like to have as low cash requirements as necessary. I am not sure about this business of paying interest. If you keep the cash requirements fairly low, in a way it is six of one and half a dozen of the other.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Gibson, if, as apparently you feel, and I am inclined to agree with you, that there should be a definition of banking, what are the implications of this? Does this mean that if a definition of banking is drafted into legislation of such a nature that all of what are now known as near banks are declared by virtue of this definition of banking to be performing the business of banking, then is the implication that they must then all become chartered banks subject, first of all, to the necessity of obtaining a charter; subject, also, to the necessity of maintaining the prescribed cash reserves and all the other regulations of the Bank Act?

Mr. GIBSON: We did not go that far in the Royal Commission's Report. We said that we thought they ought to become licensed banking institutions under the federal law. Whether they became chartered banks, or not, would depend on whether they want to apply for a charter later on; and there might still be a difference between the chartered banks and a licensed banking institution or a financial institution under federal law.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then to take, perhaps, a minor point but I think a fairly important one, if by a definition of banking a certain institution is defined as operating as a bank, would you suggest that it should be allowed to use the terms "banking, banker, bank", which are now confined to the chartered banks?

Mr. GIBSON: Mr. Cameron, if it were chartered by parliament, of course, and if it were a licensed financial institution, I do not know, but maybe that would be the difference between a licensed financial institution and a chartered bank. Perhaps there might be two stages in this. I think the word "bank" means something in this country, and I think there is merit in keeping it meaning something.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): This is the point I have in mind, that it definitely does mean something, and would your suggestion that we should make a definition of banking include giving this, I think, very valuable asset to this institution?

Mr. GIBSON: As I said, I think you might have two stages: first, a licensed financial institution and then a bank. It might move gradually from one to the other. There are some very real problems here. I do not want to understate them because, you see, some of the organizations which perform banking functions perform quite a few other functions, as well, which would be much harder to

describe as banking functions. Obviously the trust functions of trust companies are something quite apart and aside from banking functions. They are subject to provincial law, not the federal law; but then there are the banking functions of some trust companies from which they would get quite a lot of what you would call, liquid liabilities, which are close to means of payment; they have quite a lot of other liabilities which are not so liquid; they might be quite long term.

Obviously, you would have to regulate all our assets and liabilities, not their trust business as that is something quite separate. The regulations would have to apply to all our assets and liabilities which belong to the company and were in their balance sheet, or you would not have an effective regulation. This is your problem. Maybe you would fine some concerns which just had a small amount of what you would call banking business and perhaps should not be licensed as banks because you would be pulling them in by the tail, so to speak. Maybe this is a poor metaphor. There would be a common sense sort of line that would have to be drawn here.

Mr. LAMBERT: Would it be correct to say that one could introduce something analogous to zoning within the Bank Act; in other words, categories? If your fundamental idea is supervision, then one could establish categories or a type of zoning, as we are trying to do in the national parks, who are also, incidentally a problem.

Mr. MONTEITH: Not only that, but the House of Commons and the national parks.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): There is another question I would like to explore in connection with this, Mr. Gibson. Do you think there is a possibility of a development—and I am not at all sure it might not be a good development—as a result of the effects of clause 76, I think it is, which demands banks should divest themselves of their investments in other institutions, of what one might call a sort of department store operation by banks; that they would have a department which would handle much of the work, perhaps, being done now by trust companies, mortgage companies?

Mr. GIBSON: I am not quite sure I understand your question.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): There would be no prohibition, for instance, if a bank, as I understand it, were to engage in these operations as long as it was a department of their operations as a bank. There would not be investments in another financial institution. I do not know, but maybe some of my legal friends can tell me whether this is possible.

Mr. GIBSON: I can envisage the possibility of an increasingly wide range of financial services provided by banks, perhaps, more on a department basis than at present, although the branch system makes this department basis, you speak of, difficult. I am not aware that there is a proposal, at present, to give the banks trust powers. I do not think there is.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): They would not have those powers, at present.

Mr. GIBSON: So, that is an area where they, presumably, would not be operating at this time. This is one of the things we considered in the commission. We thought that, perhaps, this might wait a bit, but I know some of the banks would like trust powers. There is a very good argument that if you are going



to give the trust companies banking powers, then you ought to give the banks trust powers.

I think the sort of thing you are saying is true—that the banks have been covering a wider and wider area of financial service. First of all, they have moved out the customer; they are looking for the householder, and they have been for 20 years. They have tried to develop services, not just for the large commercial operation or the business operation, but for the householder; the mortgage business is an addition to this. They have developed the personal loan business. Now, the mortgage business fits into this; they have done something in N.H.A. mortgages but it is true that they started and then they pretty well stopped because of tight money. I think there would be a tendency to provide a broader kind of financial service and using the branch system to do this.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would this, in your opinion, tend to offset the tendency for the growth of the near banks in their near banking functions?

Mr. GIBSON: If the restrictions, at present, on the banks are removed and the restrictions which affect some of the near banks are removed, I would think that this broadening tendency would continue. These are the sorts of assumptions we are talking about, are they?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes. Then, by this means a larger proportion of the operations of our financial institutions would come under the provisions of the Bank Act and under federal control if the banks moved into these areas which are now occupied by other lending institutions, would they not?

Mr. GIBSON: I am not so sure of this. These other lending institutions have shown a lot of vitality; it is true that some of them have found the going a little tougher recently but others are doing very well indeed.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would they do as well if we had a definition of banking which brought them under the stricter supervision of the federal authorities?

Mr. GIBSON: I do not see why this would affect their progress. They get certain advantages by doing this. If you follow the kind of approach that the Royal Commission took, near banks would have certain additional powers which they now do not have as well as certain additional responsibilities which they do not presently have; certain additional requirements with regard to cash reserves and deposits and that sort of thing. How you add it all up, I am not quite sure. You might find some of the larger trust companies were pretty effective competitors.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes; I gather they have been moving into the field quite a lot, lately, have they not? This is still a minor part of their operations as yet.

Mr. GIBSON: In some cases, yes; in others, the trust companies have moved into the bank business quite a way. Some of them have just recently moved in this direction.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I am still concerned about how we are going to bring some order into the financial structure of the country

unless we can eliminate some of these other institutions by the very fact of our definition of banking; make it too onerous for them to continue.

Mr. GIBSON: I share your concern about the regulation of financial institutions. It seems to me, whether they are defined as banks or not, the problem of regulation remains and is an important problem. If you do not define them as banks then you must, some way or other, get federal-provincial co-operation to cope with this problem.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would not the definition of banking, in itself, be an assertion of federal authority over the whole range of banking operations, whether they are now within the purview of the Bank Act or not?

Mr. GIBSON: It would certainly be an act of clarification. It belongs in the federal area, I do not know, it seems to me a reasonable thing to do. I must say, Mr. Cameron, I do not think you can really be sure that simply a definition of banking and then federal regulation of the people involved in banking will solve all your regulation problems. You still have regulation problems; you still must have federal-provincial co-operation at the securities end as well as the banking end. You see banking merges into money markets, securities, short term paper, notes and all these things, and where you draw the line is very difficult. There is not an absolutely clear black and white line to be drawn here, and yet it is important that it all be regulated well.

I understand there have been discussions lately on a federal-provincial basis on security regulations which sound very promising. I do not pretend to be up to date on this, but from what I have read, it sounds as though some progress has been made here. This is important, but I do not think there is any formula by which it all can be solved. Even if you get a good definition of banking, I think you still have to have federal-provincial co-operation, if you are going to do the whole job.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I noticed in your brief, Mr. Gibson, that you express some doubts, which frankly I share, as to the effectiveness of what we have been able to find out about the government's proposals for deposit insurance. I am wondering if it would be added inducement—my theory is that you are probably right; that the ones who need to have it are the ones who will not take it—to these organizations or institutions if, in addition to deposit insurance, they were able to have access to clearing house facilities without going through a bank, as some credit unions do in my province at the present time; would this, in your mind, perhaps be an added inducement which might bring them within the deposit insurance scheme and by that means subject them to federal government supervision?

Mr. GIBSON: It is certainly another possibility, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): This would entail, of course, removing the clearing house operations from the Canadian Bankers Association to, perhaps, the Bank of Canada.

Mr. GIBSON: Yes. I do not know how important this would be; so much would depend on the terms in which they were permitted in compared with the terms under which they operate now, from a clearing point of view. There is this device and there is the deposit insurance device. I am not at all sure that this

necessarily gets people on the march. This was the concern of the Royal Commission; that it would not get people on the march.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): More likely, I would think, to get the ones who need it least.

Mr. GIBSON: I think this is pretty clear. Obviously, if you have a deposit insurance scheme, and you include the federally incorporated institutions, you have the strongest ones in the scheme to start with, or most of the strongest ones.

Mr. MONTEITH: Is this all not a little hypothetical until we have seen the legislation?

Mr. GIBSON: It is, indeed, sir. At least I am just talking; you may know more than I do.

Mr. MONTEITH: No, I do not.

Mr. GIBSON: I only know what I have read of the Minister's speeches on this subject.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It may be hypothetical, but I think probably most of us have a fairly clear idea of what it is going to be. Again, I am wondering if, perhaps, the definition of banking does not come in here, too, and that any institution that is defined as carrying on the business of banking might then be obliged to take deposit insurance. I do not know if it could be done by that means. It is probably a question for a legal opinion rather than a banker's opinion.

Mr. GIBSON: I should have thought that if you were able to define banking the deposit insurance approach would be much less important. You would get a lot of people under federal jurisdiction some of whom might benefit by it, and there would be a widening improvement, let us hope, in security regulations and a greater agreement in this area. This might cover the field not badly.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I take it that you perhaps consider it more important than some of our witnesses have indicated in the last week or so, to bring these near banks under effective supervision and regulation now, even though they are perhaps not a very important sector yet in the total financial picture and, as you say, there is some evidence that their rate of growth is declining but nevertheless, you do feel they should be brought under effective supervision?

Mr. GIBSON: I think they ought to be brought under more effective regulation.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): When you speak of more effective regulation, you speak of federal regulation, do you?

Mr. GIBSON: Not necessarily. The way this is being approached at the moment is through the federal-provincial co-operation role, and if you cannot get more people in the federal network of regulations, then this is the other area in which you will have to work.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): This would mean, in effect, I presume, that provincial authorities would be prepared to exercise the supervision that was considered by the federal authorities to be adequate.



Mr. GIBSON: Yes. You would have to have some agreement on what an adequate standard of supervision was, and there might be some delegation of supervision. But it would have to be done co-operatively.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Essentially it would be on the basis of what the federal authorities considered to be an adequate supervision.

Mr. GIBSON: I do not know. This would depend on whether you could reach federal-provincial agreement. If there were differences there would have to be a compromise.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Thank you.

The VICE-CHAIRMAN: Thank you, Mr. Cameron, I will now recognize Mr. Lind.

Mr. LIND: Mr. Gibson, at the bottom of page 5 you state:

In judging how the chartered banks would respond to a removal of restrictions, it is also worth remembering that, important as their place still is in the financial system, they have been losing relative position for twenty years.

Would you explain that to us a little more fully?

Mr. GIBSON: Mr. Lind, all I really mean here is that they have grown less rapidly than many of the other institutions. I tried to illustrate this point by showing how some of the other institutions have grown and what percentage of total assets they have accounted for in the increase in their total assets. I give the figures here from 1945 to 1964, and you get this very large increase in the proportion of assets of the financial system accounted for by the finance consumer loan companies. It rises from 1 to 7 per cent; the trust companies go up from 2 to 6 per cent; the caisses and credit unions, from 1 to 5 per cent and mortgage loan companies from 2 to 4 per cent. These institutions are all very much smaller than the banks, but they have increased their share of the assets of the financial system and the banks' share has been reduced from something like half of the total assets down to about 34 per cent.

The other institutions in the financial system which I have not mentioned here, but they are the life insurance companies, pension funds and bank and investment funds. The life insurance companies' share of the assets of the financial system have declined; the pension funds' and the investment funds' share have increased.

Mr. LIND: Let us break it down. Are the chartered banks really concerned, say, about the trust and loan companies and their position; that they have gained dollar-wise. If you break it down to the dollar increase versus what the increase the banks have had, are they really concerned?

Mr. GIBSON: I think you are always concerned if you see that your competitors are growing faster than you are. That is really what it amounts to. They have all been growing.

Mr. LIND: Let us go back to the historical position. You were on the Porter Commission and in chapter 10 states that mortgage trust and loan companies

attained a position from the 1920's to the 1930's, and then this declined in the early 1930's and they never regained that position until the 1960's. If they are just catching up on what they lost over a 30 year period, is there this terrific concern by the chartered banks over the increases which the trust and loan companies are making, dollar-wise rather than percentage-wise?

Mr. GIBSON: This is true of the trust companies. The mortgage loan companies have grown relatively larger; the trust companies have somewhat more than regained the big loss and relative position that they suffered from the 1920's to the end of the 1940's.

Mr. LIND: The Porter Commission Report stated that up until 1960 they had just gained back the ground they lost.

Mr. GIBSON: That is right. By 1960, they were about back where they were in the 1920's and they have gone a little farther since then. That is correct. But in the other cases, though, they have all reached a higher point than they ever were before. The trust companies are the only example, I think, of a group who lost ground as a result of the depression and the war and then regained it. The others have been gradually gaining ground, shall we say, in relation to the others.

Mr. LIND: Have the chartered banks not gained ground during this period?

Mr. GIBSON: No, the chartered banks have—

Mr. LIND: Have they stayed static?

Mr. GIBSON: No; the chartered banks have lost ground as a proportion of the system since the end of the war. They have gone from about half the system down to a little over a third of the system in terms of assets.

Mr. LIND: There was an item in the *Financial Post* this last week: "Another Bank joins the Higher Profit Parade", and their assets gained \$387 million last year and their profits went up by over \$1.1 million. Is that not a pretty good gain, Mr. Gibson?

Mr. GIBSON: I am not denying for one moment that bank assets have been rising; they have throughout this period. All I am talking about is rates of growth.

Mr. LIND: You have no relative rates of growth percentage-wise because if you double a small company you can have a pretty good rate of growth, but if you take it on the dollar factor, it does not amount to so much.

Mr. GIBSON: If you are saying, Mr. Lind, that the banks are still large, I am forced to agree with you.

Mr. LIND: Are they really concerned about the growth of the near banks when they come to their size and their control of our monetary system?

Mr. GIBSON: As a former banker I would say, yes, they are concerned. I do not think you could be operating a business and watch other people moving faster than you are and not be a bit concerned.

An hon. MEMBER: Not unless there was something wrong with you.

Mr. LIND: I realize there is a concern but I say that the concern, if you break it down to a factor, does not mean so much.

I would like to go over to another area here of debentures.

Mr. MONTEITH: May I just ask one supplementary here, Mr. Lind?

Mr. LIND: Yes, sure.

Mr. MONTEITH: Could this not be caused by these other institutions, which have been gaining a larger proportion of the business, offering a service to the public who, in the last run, actually decide where their business is going to go? Could it not be that these near banks and so on have been offering a service to the public which the banks have not either been able to do or have not done?

Mr. GIBSON: I think, Mr. Monteith, that you cannot find all the answers to the growth of near banks in restrictions on the banks. I think they have to take quite a lot of credit for the initiative themselves. They have gone out to find new services; they have brought in new things.

Mr. MONTEITH: They have been able to do it under the present Bank Act and other laws, possibly.

Mr. GIBSON: Sure. I think you must say that in many cases this is a real record of initiative. They have explored new fields and they have done a job. It is a mixture of these things.

Mr. MONTEITH: Thanks, Mr. Lind.

Mr. LIND: Going into the area of issue debentures, there is a subordinate security as to the banks. What is your opinion of letting the trust companies go into this field, too?

Mr. GIBSON: Are the trust companies not there now, Mr. Lind?

Mr. LIND: RoyNat is, but I am just wondering about the others.

Mr. GIBSON: Do they not issue debentures?

Mr. LIND: As subordinate to deposit and certificate liabilities?

Mr. GIBSON: I am not sure; I guess they are not subordinated, but I am not sure that they could not do that. There might be some legislative change required to do this. It might be worth looking into, but certainly trust companies and even more loan companies issue long term indebtedness, and they are not required to keep any cash reserves against it.

The VICE-CHAIRMAN: Mr. Lind, I am informed that trust companies may not issue debentures.

Mr. LIND: I asked him if he had any objection, if they were given this privilege.

Mr. GIBSON: That is right. The trust companies do not issue debentures.

Mr. LIND: I was just asking for an opinion, but the loan companies issue debentures.

Mr. GIBSON: I am sorry; yes.

The VICE-CHAIRMAN: Do you have some other questions, Mr. Lind?

(Translation)

Mr. CLERMONT: Mr. Chairman, in referring to deliberations of this Committee, I want to thank Mr. Gibson for having been so kind as to submit a brief



on which he has expressed his views, he has given us the benefit of his thirty years' experience in banking and as a member of the Porter Commission.

(*English*)

The VICE-CHAIRMAN: Does any other member have questions to ask? If not, I think I must tell the members of the Committee that next Thursday we will start with Mr. Arnold Hart, Chairman and President of the Bank of Montreal, as Mr. Gibson will not be able to be here this Thursday.

I think on behalf of everyone here—all the members of the Committee—I should thank Mr. Gibson very much for his great contribution to the evidence and to the members of the Committee. I have told the members of the Committee that Mr. Gibson has made himself available to us if later on we require his good services.

On behalf of all the members, thank you so much.

Mr. GIBSON: Thank you, very much, Mr. Chairman and Mr. Clermont. I appreciate the opportunity of appearing before you and I have found it most interesting and stimulating, if at times, perhaps, a little too stimulating. Thank you.

The VICE-CHAIRMAN: This Committee is adjourned until next Thursday at 11 a.m.

**APPENDIX "R"**

Submission to the

House of Commons Committee on Finance, Trade and Economic Affairs,  
regarding Bill C-222, an Act respecting Banks and Banking.

(By J. Douglas Gibson)

I have asked to appear before the Committee on Finance, Trade and Economic Affairs as a former banker and one-time economist. I am speaking as an individual, and not on behalf of the banks or the Royal Commission on Banking and Finance of which I was a member, though I was and am in full agreement with the Royal Commission's report.

This is the second occasion in about twelve months when I have requested the privilege of appearing before your Committee and this time my comments will be briefer than they would have been with regard to the earlier bill. The reason for this is that the importance of a competitive financial system is more fully recognized in the bill before you now. The bill proposes removal or lessening of restrictions on banks to compete—in its approach to the interest rate ceiling, in its differential treatment of reserves against demand and notice deposits, and in its provision for more rapid entry of the banks into the mortgage business. While in the present inflationary environment these measures cannot be expected to be rapidly effective, they are of profound importance in establishing an appropriate background and climate for a more competitive and flexible financial system.

My own experience and the events of recent years have convinced me that in the kind of world in which we live competition is the best assurance of efficiency. I am sure this applies in finance as well as in other forms of business. Certainly, as a country we have very largely accepted the competitive approach in our international economic relations. Since the middle thirties, when we (and the Americans) began to turn away from protection, we have been gradually moving toward freer trade and a more open type of economy. Apart from the special conditions of the last war and a few crosswinds and reverses, Canada has consistently pursued freer multilateral trading arrangements for almost thirty years. We have done this not only because of the interests of farming and the other staple industries but because it was also the only effective path toward the development of efficient secondary industries. First-class secondary industries in many cases need to be specialized to be efficient and in most cases need broader markets than are available at home. This is particularly true with the rapid advance in technology characteristic of the times and with the increasing emphasis on sales and engineering service. It is no accident that the few smaller countries that have managed to remain in the van as manufacturers, such as Sweden, Holland and Switzerland, have specialized in certain branches of manufacturing, not excluding some highly complex operations, and have generally been low tariff economies.

In other words, we have found it in our national interest to permit freer movement of goods, money and indeed people across our borders. We have sought and succeeded in promoting economic efficiency and higher living standards for all through open competition rather than by protecting special groups. It is encouraging to see that this principle is now being applied in the sphere of

finance where restrictions particularly on the chartered banks have had the effect of protecting certain other financial institutions against competition within our own economy and, what is of even more importance, of denying access to cheaper forms of finance to many smaller borrowers. In the postwar period, the chartered banks have shown increasing interest in developing term-lending business with small and medium-sized concerns who find it impracticable to go to the capital market. In recent years, however, what would otherwise have been a developing trend has been checked by the combination of a rising cost of money to the banks and a fixed ceiling on what they may charge. Money has been available for such borrowers at rates usually much above the 6 per cent ceiling, particularly from the finance companies who have had the initiative to move into and to some extent to fill this important gap in the capital market. It should also be added that the Industrial Development Bank has been operating in this area at rates consistently above 6 per cent for over seven years. The raising and ultimate removal of the interest rate ceiling envisaged in the bill before you will gradually make more funds available for small and medium-sized business and because of the added competition will reduce average rates to the important group of borrowers concerned.

Here, once again, I should like to make a more general observation which is that the growth of small and medium-sized businesses into medium-sized and large businesses is the process by which a competitive system renews and sustains its strength. There must always be new candidates ready to move in when the older and larger businesses show lessened vitality and efficiency. For this reason it is important that the financial system should provide funds for such development at the lowest feasible cost. The interest rate ceiling applicable to the chartered banks has been keeping the cost higher than it need be for no good reason.

Similarly, the high cash reserve requirements against all forms of deposits with the chartered banks have been unnecessarily reducing the ability of the banks to compete for savings and term deposits. The reduction in the cash reserve requirements on notice deposits and the provision for debenture financing will help the banks to compete more effectively for the term funds needed to support the desired expansion in term-lending activities in coming years. The writer must admit, however, to some puzzlement over the proposed increase in the cash requirements against demand deposits since the present requirement is already sufficient from a practical point of view and since no action is planned to apply reserve requirements to the demand deposits of near-banks. Another feature of the bill which will make for a healthier more competitive environment is provision for the more rapid (but still gradual) entry of the chartered banks into the mortgage business than that envisaged in the preceding bill. All these changes will help in moving toward the more efficient and productive economy which we all desire.

In assessing what is likely to happen when and as you move to increase competition as proposed in the bill you should judge how you think the changed incentives are likely to work—how you think the banks are likely to act in pursuing their own interests. It is not a question of whether their intentions are good though I think the record suggests that the banks are good corporate citizens. It is rather a question of how they would respond to the hope of profit and the fear of loss. The price system, the market system, the competitive



system, whatever you like to call it, is a profit and loss system and institutions should respond accordingly. Is it in the banks' interests to go further in term lending to small and medium-sized businesses? They have a good deal of knowledge as providers of working capital to these businesses already. They have the wide representation. They might need some more specialized personnel. If they could see a profit after reasonable provision for loss why would they not push ahead in this area? The banks in fact found a way to make a profit on consumer lending and the record speaks for itself. They did lower interest rates and improve the facilities available in this whole area of lending. Is it in the banks' interests to go into the conventional mortgage business? Again, the answer is yes, if it can yield a reasonable profit. Some banks might put more emphasis on business term-lending and others on, say, residential mortgages. It depends on their assessment of how they can best use their resources of management and capital. In a competitive economy, institutions will and should do the thing which yields the best earnings. If artificial barriers prevent them from seeing a reasonable profit in a particular type of lending they will not and they should not engage in it.

In judging how the chartered banks would respond to a removal of restrictions, it is also worth remembering that, important as their place still is in the financial system, they have been losing relative position for twenty years. In 1945 the banks accounted for 49 per cent of the assets of the main financial institutions, whereas in 1964 the proportion was down to 34 per cent and since then it may have dropped a little more. Over the period from 1945 to 1964, the percentage accounted for by the finance and consumer loan companies rose from around 1 per cent to over 7 per cent, while the proportions for the trust companies rose from 2 per cent to 6 per cent, for the caisses populaires and credit unions from 1 per cent to 5 per cent, and for the mortgage loan companies from 2 per cent to 4 per cent. In total this group of financial institutions increased their share of the system from 6 per cent to 22 per cent. Needless to say, these are not trends which bankers view with equanimity. Some movement in this direction was probably inevitable with the growth and increasing diversity of our economy. It must also be recognized that the initiative and ability of this rising group of institutions has had much to do with their success. But when all this is said, a good deal of the change reflects the protection that the "near" banks have enjoyed against the chartered banks. So there is an added edge to the banks' desire to compete—they do not relish the persistent decline in their relative position.

However, while the bill before you takes a long step toward a more competitive system, there are some aspects of it which in my view are not in harmony with this approach. I would refer in particular to section 76 which would introduce and make retroactive a provision that banks should not own more than 10 per cent of the voting stock of other institutions. It is one thing to pass legislation designed as protection against a degree of concentration that might limit competition. It is quite another thing to require the undoing of ties of ownership which have thus far, at least, enhanced competition. There can be little question that the competition amongst the trust companies and between the trust companies and other financial institutions including the banks has increased during the time that certain banks have acquired interest in trust companies. The whole situation has been stirred up and has become more

competitive. And yet the banks which took such action are to be asked to undo it in less than five years, and no reason is advanced nor is any evidence brought forward to suggest that the relationships which it is proposed to undo have been restricting or are likely in future to restrict the state of competition in the financial business.

In this general connection, I would also point to the evident fact that the initiative of some banks has contributed to better services and lower costs to the community in the area of mortgage insurance and term lending to business. Even though the banks concerned do not have controlling interests in these new ventures, they would under the present legislation be required to reduce such interests to 10 per cent of the voting shares. To what purpose? Why should not the backers of good ideas reap some return for their initiative? Do we want institutions to initiate, to promote and to develop new ideas and new and improved ways of doing things? If so, we should encourage such initiative, not remove the incentives.

A further element in the bill which does not fit the competitive prescription which I have been advancing is the portion concerning foreign banks. I refer to clause 53 concerning ownership of banks which, in effect, appears to prevent non-residents from starting a bank in Canada.

Like many others, I recognize that Canada has special problems being so close to such a big neighbour. The concentrations of economic power of which the great American banks are a central feature are formidable and I for one should not want to see the large Canadian banks owned in the United States. At the same time, it seems to me that it is much better to say, as the Royal Commission on Banking and Finance proposed, that foreign banks and their associates should not be permitted in future to purchase stock in existing Canadian banks. We should not close the door completely on non-residents wishing to incorporate banks, nor should we bluntly refuse representation of foreign banks in this country. This is out of keeping with the mainstream of Canadian policy and against our basic interests. The Commission believed that it was appropriate to permit agencies of foreign banks in the main financial centres on a similar basis to that permitted foreign banks in New York, provided the government felt they had something useful to contribute to the competitive scene.

Apart from the general argument, I could make further comments from my banking experience. Several of the Canadian banks have substantial representation abroad and are concerned to be treated reasonably in the countries where they operate. I do not think it is any exaggeration to say that the Canadian banks have really accepted the challenge of competition abroad, of keeping up with the big fellows in the international sphere. For example, of the fifty largest banks in the world five are Canadian and at the present time approximately 19 per cent of the assets of Canadian banks as a group are denominated in foreign currencies. Certainly the expansion of Canadian banking abroad has been pronounced in the last ten years and the Canadian banks are, in fact, making a growing contribution to Canada's foreign trading and investment interests. The banks do not want to see precedents created which might be the excuse for discrimination against them abroad, in the United States or anywhere else. And I would remind you that in the United States the idea of reciprocity in the treatment of banks seems to be becoming well established and is reiterated in a recent study done for the



Joint Economic Committee of the U.S. Congress.\* The foreign business of the Canadian banks is useful to Canada in promoting trade and financial relations and also to some degree in producing profits which add to Canadian taxes and to Canadian supplies of foreign exchange.

There is one major remaining point that I wish to make. It concerns the importance of a national approach to banking legislation. The proposals of the Royal Commission on Banking and Finance that banking be defined, and that institutions engaged in banking as defined be subject to national supervision and monetary control, find some reflection in the Government's approach but in my opinion not nearly enough. The need for a national code for banking activities is much more evident today than it was when the Commission's report was published. Somehow, we must get a national system of supervision and inspection, or its nearest equivalent through federal-provincial agreement.

To get a national system of supervision, we have to decide what are banking activities. This the Commission endeavoured to do and came to the conclusion that the type of liability dealt in, how close a substitute it was for money, was the prime criterion. The Commission drew certain lines to divide banking liabilities from non-banking liabilities and indeed decided that deposits of up to 100 days maturity should be regarded as banking liabilities. This was an arbitrary decision and, though I think it was a sensible one, there may be a better and more practicable line. What is almost beyond debate is that banking must be defined in terms of liquidity of the liabilities concerned and that it is simply a question of drawing a reasonable line—perhaps a conservative line at first but some definite line. The old criterion that a bank was an institution with the privilege of note issue disappeared as the Bank of Canada took over this function, and nothing has been done since to set out a reasonable definition. Once banking is defined more or less precisely, so that everyone knows what banking is, it will be possible to identify those financial institutions which fall within the provisions of the British North America Act relating to banking which is an area assigned to the federal authorities.

The Minister's speech and the legislation before you give no indication that an attempt is to be made at this time to define banking. Rather the effort to improve supervision appears to take the form of closer federal-provincial cooperation and of setting up a deposit insurance agency which would apply national standards of supervision to all concerns whose deposits were insured. Closer federal-provincial cooperation in this whole area of financial regulation is highly desirable and I would hope and expect that real improvement could be achieved. I am doubtful, however, whether federal-provincial cooperation is a substitute for a serious attempt to define the federal government's responsibilities in this field, and I would have thought indeed that such an attempt was a necessary step to improved arrangements between the federal government and the provinces. The grey area between federal and provincial jurisdiction now inhabited by the so-called "near" banks has been the area where the most rapid expansion has been occurring and to leave it grey may well leave a bigger problem for the future which might ultimately become a problem of monetary control as well as one of supervision.

\*Economic Policies and Practices, Paper No. 9, Foreign Banking in the United States, prepared for Joint Economic Committee, 1966.



Perhaps the grey area will not widen in future. Perhaps the "near" banks will not grow relatively as quickly as they have been growing in recent years. Perhaps a national system of deposit insurance will attract a large number of "near" banks into a federal system of inspection. Undoubtedly a deposit insurance scheme if the rates are fairly low would be attractive to some of the "near" banks. For a moderate fee and the acceptance of supervision, they would be in a position to compete on terms of equal security (up to a stated deposit limit) with the strong and well-established institutions. Such an offer might not interest the larger and stronger of the "near" banks any more than it would interest most of the established chartered banks, and it certainly would not interest concerns whose activities were border-line or irresponsible. But it might very well interest many institutions between these two extremes.

If a deposit insurance approach is to be successful, it must somehow apply adequate standards of supervision to most of the "near" banks which are not now receiving appropriate supervision. Many such institutions might indeed welcome the application of such standards of supervision and the stamp of approval that would go with them. Some, however, might feel that their freedom of action was being hampered or that their ability to make a sufficient margin was being unduly restricted. There is the real risk that those who needed supervision most would be agile in avoiding it. If the provinces actively supported the idea of a national deposit insurance and supervisory approach, the chances of a wide response would be much improved.

There is also the very important question of coverage and rates. The Minister of Finance has indicated that the "banks and other federally incorporated institutions would be required to have their deposits insured" and that the deposit insurance corporation "would be authorized to insure the deposits of provincially incorporated institutions where this was desired by the institution and the provincial government concerned". It so happens that the largest and strongest institutions, the chartered banks, are federally incorporated and as a group have less need of deposit insurance than any other financial group. The federally-incorporated institutions make a good base for an insurance scheme. If they are to be included on a compulsory basis, what are the terms to be offered those that enter on a voluntary basis with provincial approval? Are weaker and less-tested institutions to be afforded rates relatively low in relation to the risk? If this were so, the experienced banker, and I count myself as one after thirty-odd years in one of the banks, might well wonder why it was being made fairly easy to duplicate the sense of security for the depositor which in the past was gradually developed as a result of good management, the accumulation of reserves, the weathering of crises, and everything else that goes into building a good reputation.

It would be easy to start a new federal deposit insurance corporation, and a successful one financially, which in effect insured on a compulsory basis the deposits of the chartered banks and the limited number of other deposit-taking institutions incorporated under federal law. This would achieve comparatively little except to help new chartered banks, and would in effect represent a new tax on the strong and well-established. It might not be too difficult to get a broader coverage by enticing "near" banks now operating under provincial charters into a federal insurance scheme with low rates, provided the provinces did not oppose such a policy. But this would be unfair to those institutions who had

built their reputations the hard way and in any case it would not bring in the corner-cutters and borderline concerns that are most in need of attention. Other questions also arise. What about the credit unions and the caisses populaires? These are important deposit institutions. Would deposit insurance be available to them?

In any case, we should be under no illusions that there exists a real problem of financial regulation. The revelations of sloppy and irresponsible conduct before the Hughes Commission in Ontario while they make sensational reading tell a very disturbing story about what has been happening in parts of our financial system. There are serious problems of liquidity and security which remain. The quality of credit has gradually deteriorated in recent years. Perhaps if we allowed unrestricted competition and let the devil take the hindmost, the problem would in time solve itself. But the cost would be high and we simply do not do things this way. We say the public should be protected—that there should be supervision in the public interest. In that case, we should improve the supervision and I cannot honestly say that I think the present prescription is sufficient.

I should be glad to answer questions or to develop the reasoning presented in this statement.













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*The Clerk of the House.*

HOUSE OF COMMONS

First Session—Twenty-seventh Parliament

1966

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STANDING COMMITTEE

ON

FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. HERB GRAY

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MINUTES OF PROCEEDINGS AND EVIDENCE

No. 28

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THURSDAY, DECEMBER 1, 1966

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Respecting

Bill C-190, An Act to amend the Bank of Canada Act,  
Bill C-222, An Act respecting Banks and Banking.  
Bill C-223, An Act respecting Savings Banks in the Province of Quebec.

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WITNESSES:

G. Arnold Hart, President, Bank of Montreal; C. F. Elderkin, Inspector  
General of Banks.

ROGER DUHAMEL, F.R.S.C.  
QUEEN'S PRINTER AND CONTROLLER OF STATIONERY  
OTTAWA, 1966

STANDING COMMITTEE  
ON  
FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. Herb Gray

*Vice-Chairman:* Mr. Ovide Laflamme

and Messrs.

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Basford,	Flemming,	Lind,
Cameron ( <i>Nanaimo-</i>	Fulton,	McLean ( <i>Charlotte</i> ),
<i>Cowichan-The Islands</i> ),	Gilbert,	Monteith,
Cashin,	Irvine,	More ( <i>Regina City</i> ),
Chrétien,	Lambert,	Munro,
Clermont,	Lamontagne,	Valade,
Coates,	Latulippe,	Wahn—(25).

Dorothy F. Ballantine,  
*Clerk of the Committee.*



## MINUTES OF PROCEEDINGS

THURSDAY, December 1, 1966.

(55)

The Standing Committee on Finance, Trade and Economic Affairs met at 11:20 a.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Cameron (*Nanaimo-Cowichan-The Islands*), Chrétien, Clermont, Comtois, Fulton, Gray, Laflamme, Leboe, Monteith (9).

*Also present:* Messrs. Grégoire, Johnston and Richard.

*In attendance:* Messrs. G. Arnold Hart, President, Bank of Montreal; and C. F. Elderkin, Inspector General of Banks; Miss M. R. Prentis, research assistant.

The Committee resumed consideration of the banking legislation.

The Chairman introduced the witness, Mr. Hart, who read his brief. In accordance with the resolution passed at the meeting of October 13, 1966, the brief is attached (*See Appendix S*).

The witness was questioned and at 12:55 p.m. the Committee adjourned until 3:45 p.m. this day.

### AFTERNOON SITTING

(56)

The Committee resumed at 4:00 p.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Cameron (*Nanaimo-Cowichan-The Islands*), Chrétien, Clermont, Comtois, Fulton, Gray, Laflamme, Leboe (8).

*Also present:* Messrs. Grégoire and Johnston.

*In attendance:* The same as at the morning sitting and Mr. Denis Baribeau research assistant.

The Chairman referred to two papers prepared by the research assistants in answer to questions raised by Mr. Clermont, entitled respectively *Bank Service Charges and Instruments Eligible for Re-discount at Federal Reserve Banks*. The Clerk was directed to have copies made and distributed to the members.

Reference was also made to an extract from the Congressional Record of the United States Senate entitled *Foreign Banking Control Bill; Uniform Regulation of Foreign Banks*, and the Clerk was directed to distribute copies to the members.

The questioning of the witness was continued and concluded.

At 6:18 p.m. the Committee adjourned until Tuesday, December 6, 1966 at 11:00 a.m.

Dorothy F. Ballantine  
*Clerk of the Committee.*



## EVIDENCE

(Recorded by Electronic Apparatus)

THURSDAY, December 1, 1966.

The CHAIRMAN: Will the meeting please come to order. At the moment we will proceed unofficially for the purpose of taking evidence, with the usual proviso.

Our witness today is Mr. Arnold Hart, President of the Bank of Montreal. I will now invite Mr. Hart to make his presentation. As the Committee knows, our procedure has been to ask witnesses to do no more than summarize their briefs because they have been distributed to the Committee some days before. It may well be that the Committee would find it equally convenient if Mr. Hart read his brief because it consists of only four double spaced pages. To ask him to summarize his brief might take just as long as asking him to read it. If the Committee is in agreement with this I would now invite Mr. Hart to present his brief to us.

Mr. G. Arnold HART (*President of the Bank of Montreal*): Thank you very much, Mr. Chairman. May I say first of all that I welcome the opportunity to appear before this distinguished Committee. I understand that any member of Parliament may come in and ask questions. It is a bit like appearing before the Ottawa Rough Riders, who have power to add numbers to their team, you may try to overcome me by sheer weight of numbers.

The CHAIRMAN: Sir, to bring you a sense of some relief, may I say that that power is subject to the overriding control of the formal members of the Committee.

Mr. HART: Thank you, Mr. Chairman. I will leave it to anyone else to draw any analogy they like between the name of the Grey Cup and the name of our distinguished Chairman but, at the same time, it may be fitting to say that things are not all black or white; there is a little bit of a grey area in everything.

Mr. Chairman, and gentlemen, I will with your permisison, in as much as my brief is not too lengthy, read the text for the record. (*See Appendix S*).

If I may comment further, Mr. Chairman, at this point with your permission, I would like to make one or two other references. I strongly suspect that if the capital cost of the Mercantile had been acquired by a bank, say, in France, in the United Kingdom or in almost any other country except the United States, the legislation proposed might well not have been introduced at all. Gentlemen, there is a question of fair play in this and one does not change the rules in the middle of the game. A corporate entity acting within existing legislation has the right to full protection, by law, under the act embodying such legislation.

Mr. Chairman, that is all I have to say at this point.

The CHAIRMAN: Thank you, Mr. Hart. Before recognizing the members of the Committee in the usual manner for the purpose of placing questions to you, I



should state, as you are aware, that once we have dealt with the topic or topics raised in your brief you will, of course, be available for questioning on any other topics relevant to the legislation referred to us for our study and recommendation.

I think the Committee will agree that there really was only one basic topic raised in your brief, the general question of operation of banks within the banking industry in Canada by non-residents, with particular reference to the one bank referred to by Mr. Hart. In that regard, it would be in order now, to begin our questioning. I would recognize, first, Mr. Clermont, followed by Mr. Monteith, Mr. Laflamme, Mr. Cameron and Mr. Leboe.

*(Translation)*

The CHAIRMAN: Mr. Clermont you have the floor.

Mr. CLERMONT: Mr. Hart in your last remark, you say that if the Mercantile Bank were controlled by British or French interests, there would be no suggestion such as that proposed Bill C-222 of 75 (g). This is a hypothetical question, is it not?

*(English)*

Mr. HART: Mr. Clermont, that is correct.

*(Translation)*

Mr. CLERMONT: I do not know, Mr. Hart, whether you are ready to admit this. Let us assume we have a bank which is controlled by American interests. This, for Canada, represents dangers which are not the same as if the capital were provided by France or Great Britain, or other countries. In this country we have a great many companies whose head office happens to be in the United States. I will give you an example. Supposing the First National Bank or the Chase National Bank of New York were to be the bankers of General Motors in the United States. Let us assume further that this bank were to ask the Parliament of Canada for a charter and would ask officially or otherwise, General Motors of Canada to bank with it in Canada. What would General Motors do in this instance? This is part of Question 2 of course, but what would you think would happen?

*(English)*

Mr. HART: I realize that your question is hypothetical but I do submit that an organization of the size of General Motors would continue to deal with many banks, as it does at the present time. I cannot tell you offhand how many banks they deal with in the United States but they certainly deal with a number of banks in Canada. I do not think that General Motors would want to get themselves into a position where they are dealing solely with one bank. That is not the pattern of larger corporations in the United States. They deal with many banks in many cases.

*(Translation)*

Mr. CLERMONT: You will understand of course, Mr. Hart, that I mentioned General Motors as an example. But the case may be the same for hundreds of other companies in Canada, Singer Sewing Machine Co. for instance. My second question is as follows. You have a branch in New York, you have another branch in San Francisco, an agency or a branch, at any rate—

(English)

Mr. HART: We have an agency in New York and we have a wholly owned subsidiary in California.

(Translation)

Mr. CLERMONT: Are these institutions entitled to receive deposits from American citizens?

(English)

Mr. HART: Because of the laws under which we operate our New York agency, we are not permitted to accept deposits from firms and individuals resident in New York State. There was no prohibition whatsoever against our taking deposits from residents of any other state in the union. We could take deposits from Connecticut and New Jersey, for example. But as a matter of fact we do not really because we are not down there to compete to that extent with our American banking friends. But there is no prohibition against our taking deposits from residents outside New York State. In California we operate exactly as any other bank out there chartered under California state law, and we are free to do exactly as any other bank does.

(Translation)

Mr. CLERMONT: This means that in the case of your New York agency, there is some discrimination. You are not entitled to accept deposits from residents of the State of New York, whereas here in Canada, when Parliament grants a charter to a group or other to carry out banking operations in this Canada, it obtains the same privileges as any other bank. All other banks, in other words, may accept deposits from any resident of Canada.

(English)

Mr. HART: Mr. Clermont, that is correct. Dealing with the first part of your question, when we commenced operations in New York we did not regard this as discrimination, and we do not now because those were the rules of the game when we established our agency, and we have continued to operate, as I said, for 107 years under those rules unchanged.

The CHAIRMAN: Is it correct that as an agency in New York you are now under greater regulations by the United States Federal Reserves System.

Mr. HART: No, we are not, Mr. Chairman.

The CHAIRMAN: Are you making greater returns to the United States government?

Mr. HART: No, we are not, Mr. Chairman. We are subject to examination by state bank examiners, but we are not subject to any additional restrictions under this one which I have been mentioning.

The CHAIRMAN: Are you making a greater number of returns or reports to the United States authorities than you did, say, a year ago?

Mr. HART: No, not to my knowledge, Mr. Chairman. As I say, we are examined regularly once a year by the inspectors of the state banking authority. It is a surprise audit. We also carry out our own audit in conjunction with our shareholders' auditors. But so far as the United States is concerned, we are subject to the same examination as any other bank operating in New York State.

The CHAIRMAN: You are telling us that in the past, say, two years, your agency in New York has not begun to provide a greater amount of information to the United States Federal Government or Central Banking Authority.

Mr. HART: Mr. Chairman, to my knowledge that is correct. I think it is perhaps true that the bank examiners are looking more closely at the operations of banks generally in New York. Now they are not singling out the agencies of any foreign banks to any special degree to which I am aware.

*(Translation)*

Mr. CLERMONT: I believe Mr. Hart, you have an agency in the United Kingdom in London? Do you have another one in France also?

*(English)*

Mr. HART: In London we have two branch offices, Mr. Clermont, which operate as branches of the Bank of Montreal, not as agencies. We are quite free of course to operate within the laws of the United Kingdom.

*(Translation)*

Mr. CLERMONT: Are you entitled to receive deposits from the United Kingdom citizens?

*(English)*

Mr. HART: Yes, sir, we are, and in fact do.

*(Translation)*

Mr. CLERMONT: Under what authority do you operate? How are you incorporated there? How do you receive your operating permit from the United Kingdom?

*(English)*

Mr. HART: Mr. Clermont, you will perhaps realize that in the United Kingdom there is nothing comparable to our Bank Act; they operate under company law. Therefore, in establishing a branch, it was just like any other organization going in and setting up operations in the United Kingdom. There was nothing to prevent us from doing so.

*(Translation)*

Mr. CLERMONT: Do you have an agency or branch in Paris, or any other city in France?

*(English)*

Mr. HART: We do not have an agency in Paris. We have what we call a special representatives office in Place Vendome which is really a business development office, but we do not do a banking business. However on the continent we do operate now seven branches for the NATO forces at air force and army installations, but we deal solely with members of the armed forces and their dependents. We do not do any business with citizens or nationals of the country either in Germany or in France.

The CHAIRMAN: Why is that?

Mr. HART: Because we set up the operation solely to look after our army and air force requirements over there, and to assist their dependents. We are actually



operating right on the bases and, therefore, we do not have any contact with the outside public.

The CHAIRMAN: Would you be entitled to do so under French or German law, if you wanted to?

Mr. HART: Sir, I cannot answer that question because we have not looked into it. Our sole purpose was to serve the Canadian armed forces and their dependents.

*(Translation)*

Mr. CLERMONT: According to the answer you gave to one of my previous questions, in respect of your agency in the City of New York, it would appear that the only operations that particular agency carries out are exchange operations and international operations?

*(English)*

Mr. HART: Mr. Clermont, that is a very narrow definition. Yes, we do a very substantial exchange business. We also do a substantial securities business. We make loans down there, and we are a factor, along with other foreign bank agencies, particularly in the call loan market. This is really for the purpose of employing our surplus United States funds for short term investments.

*(Translation)*

Mr. CLERMONT: You mentioned the fact that you granted loans but you are not entitled to accept deposits from citizens of the State of New York, but you are entitled to accept deposits from any other person not resident in the State of New York. Now, as I remember correctly, you also mentioned the fact that you had no deposits from these people, even though they were entitled to it?

*(English)*

Mr. HART: Oh, you mean deposits from residents of other than New York State. No, I cannot recall a case where we had a deposit in our New York Agency from residents outside the State of New York. Mr. Clermont, I was going to add that we do, of course, have deposits in U.S. dollars in Canada from residents of New York State and other states.

*(Translation)*

Mr. CLERMONT: Which would mean that if you made loans to American citizens, these would come from deposits made by Canadian depositors or American depositors in Canada?

*(English)*

Mr. HART: They could come from both sources. To clarify this somewhat, we do not engage in a loaning business in our New York agency to the extent that we do in Canada. Our main purpose down there is to operate in the call loan market and to employ for short term purposes surplus U.S. funds which are not otherwise required at that particular time. And we, along with agencies of other foreign banks, as I say, are quite a factor in the call loan market in New York city.

*(Translation)*

Mr. CLERMONT: In your brief, Mr. Hart, you object very strongly to Clause 75(g) of Bill C-222. Are you ready to indicate what you think of Section 53,

which is pretty much along the same lines. It is not quite the same thing, but it does deal with shares held by non-residents in a Canadian bank which would not go beyond a 25 per cent proportion, or 10 per cent, as the case may be? This is Clause 53(2) (a)?

*(English)*

Mr. HART: Mr. Clermont, I must say that I am opposed to any restrictions placed on the international operations of banks. After all, banks have been in this business for many, many years—in our case nearly 150 years. We have never been hampered in our operations abroad by restrictions imposed upon us, and even though we may have gone in with certain rules laid down we accepted those rules and continued to operate. Subsequently, there have been no restrictions to my knowledge that have been imposed, as I mentioned earlier in answer to one of your questions.

I think to restrict ownership in the international field is a backward step. To relate this to the Mercantile Bank of Canada, I think we are talking about two different things, Mr. Clermont, because in this case we have a chartered bank which received its charter from the government of Canada and it operated with full powers as a chartered bank under the existing Bank Act. To say now that we are going to change the rules for that bank is the point to which I raise the objection. If a future decision is made that such restrictions as are put into Section 53 and elsewhere shall govern, and if that is the law, that is fine. Then everybody else will operate under the same law—that is, everybody else who wants to come into Canada. But I submit it is wrong in principle to change the rule now for a legal entity which is operating within the law.

*(Translation)*

Mr. CHRÉTIEN: A supplementary question, Mr. Hart. Are you aware of the fact that the Bank in question had been advised of the intentions of the Government in this respect? Are you aware that it had been informed of the suggested changes that the Government had in mind at the time?

*(English)*

Mr. HART: I am aware only to the extent that I read about this in the press. Obviously one could draw the conclusion that they were warned that such action might be taken. But notwithstanding that, they were a chartered bank operating within the law, and I think to single them out for special discriminatory legislation is bad law.

*(Translation)*

Mr. CLERMONT: My last question, Mr. Chairman, is as follows. You mentioned, Mr. Hart, that when the Mercantile Bank of Canada had put a request to the Parliament of Canada for a charter you had, of course, no objections whatever. Would you feel the same way if another group of non-residents were to ask Parliament for the right to operate a banking business in Canada? Would your bank have any objection to that?

*(English)*

Mr. HART: Mr. Clermont, under the existing Bank Act I think there would be no right to oppose another bank attempting to establish an operation in Canada. The rules obviously may change when this revision goes through. But

under present law, and because our banking—and I think other banks would support the fact too—operations abroad never have been inhibited, we can hardly expect to receive treatment in other countries which we are not prepared to accord in this country.

(Translation)

Mr. CLERMONT: You did admit, however, that in the State of New York there is a certain amount of discrimination but that you accepted that state of affairs?

(English)

Mr. HART: Mr. Clermont, we accepted that when we established our agency 107 years ago, and we have operated since. There is only the one restriction.

The CHAIRMAN: Mr. Hart, before recognizing Mr. Monteith I would like to ask you a quick question. When was your bank first created in Canada?

Mr. HART: On November 3, 1817.

The CHAIRMAN: Have the rules of the game changed for the banking industry in Canada since 1817?

Mr. HART: We have had several Bank Act revisions, Mr. Chairman. Yes, I would submit that they have changed.

The CHAIRMAN: Have you come before a parliamentary committee or the Parliament of Canada to object that parliament was trying to change the rules of the game and said that you should be permitted to operate in the same way as you did in 1817 because you were incorporated then?

Mr. HART: Oh, no, sir. I think we are talking about two different things. The purpose of the Bank Act revision, as I understand it, is to update the legislation and the provisions in the Bank Act so that the banks hopefully can continue to play a better part in the economy of the country generally. I think we are the only country in the world that has a Bank Act that comes up for decennial revision, and the bankers welcome this because it does give an opportunity to tidy up legislation which may have become outmoded because of the passage of time and other developments in the country.

The CHAIRMAN: Have you always been completely in accord with every one of the proposed changes since 1817?

Mr. HART: I cannot say that, sir, no. There are some things that we would like to see done and perhaps some things we would not like to see done. The law is the law and we abide by it.

The CHAIRMAN: I gather that you have never come to parliament and said that the rules were such and such in 1817; we like them and we want to be able to live under them because we were incorporated then.

Mr. HART: I was not around in 1817.

The CHAIRMAN: I do not mean you personally, your organization.

Mr. HART: No, I think it is always the endeavour of the chartered banks to co-operate with the government in devising a bank act which we feel is suitable to the conditions of the country at that particular time. It is co-operation, I



assure you. Naturally, we are not always happy with certain legislation which may be introduced. Of course we have cases in point here. There are other things we would like to see done. If it is in the wisdom of parliament that the Bank Act should not be so changed, then we accept that and we abide with the rules as laid down.

(Translation)

Mr. GRÉGOIRE: A supplementary question, Mr. Chairman. Since non-resident interests who have bought the Mercantile Bank of Canada were advised at the beginning of this purchase that the Government intended taking such steps as are provided for under 75 (g) (2), do you not feel that that was sufficient warning? Did you not think that they were made aware of certain provisions in the Bank Act? Does this constitute discrimination according to you?

(English)

Mr. HART: Mr. Grégoire, I am at a disadvantage because I have not seen any official documents stating the warning. All I have seen was what was in the press.

The CHAIRMAN: Mr. Hart, I think at this point it would be convenient for me to read into the record from *Hansard* of Monday, June 14, 1965, at page 2372. This is the official verbatim record of the House of Commons of Canada. I am quoting from a speech of the Hon. Walter Gordon, then Minister of Finance. Referring to a meeting that he had with representatives of the First National City Bank, Mr. Gordon said:

I informed the representatives of the First National City Bank that normally it would be unfair to apply retroactively any legislative restrictions on control of banks by non-residents. However, I said that since the First National City Bank were now aware of the Government's views, and had not at this time purchased control of Mercantile, the Government would not consider they were entitled to any special exemption from legislation in respect of foreign ownership that might be brought down in the future.

After a very full discussion, I advised the representatives of the First National City Bank of New York not to proceed with their proposed action until after the Bank Act was revised. There was no misunderstanding on the part of any of those present as to exactly what was meant. The representatives of the First National City Bank of New York were given clear notice of the Government's views. They were forewarned about the kind of legislation that might be expected when the Bank Act came up for review. I pointed out that Mr. Rockefeller and Mr. McFadden had sought an interview with me to ascertain the views of the Canadian Government before proceeding with a certain transaction. They had now been informed of the Government's views in categorical terms.

That is the end of the quotation that I wanted to read. There are other comments before and after which I could read.

(Translation)

Mr. CHRÉTIEN: A supplementary question, Mr. Chairman.

The CHAIRMAN: I must interrupt you for the moment, Mr. Chrétien. I think we should be fair, as Mr. Monteith is next on my list.

Mr. CHRÉTIEN: I really have not taken up too much time in the Committee.

The CHAIRMAN: I am ready to accept your supplementary question, but to be perfectly fair to our colleague, Mr. Monteith, I simply want to point out that if we spent too much time on supplementary questions it would not be a good thing. However, if Mr. Monteith wishes to yield, I will accept your supplementary question.

*(English)*

Mr. MONTEITH: Mr. Chairman, I do not mind yielding at this time.

*(Translation)*

Mr. CHRÉTIEN: Mr. Hart, when your bank is in the State of New York or in California or elsewhere, you attempt to behave as good citizens of those states, do you not?

*(English)*

Mr. HART: If I understand your question correctly, you are asking would this apply to an operation which was now in being in a state in the United States? Or is your question intended to imply where we are not operating in a state now but wish to do so?

*(Translation)*

Mr. CHRÉTIEN: And what would be your attitude if you were advised by the financial authorities of the states involved, not to proceed under the circumstances because there was a forthcoming revision of banking legislation in a given state? Would you continue, or would you not?

*(English)*

Mr. HART: This is a rather hypothetical question because, to my knowledge, we have not encountered anything of this sort up to the present time with our foreign operations. It is difficult to pose a hypothetical matter here, but if we were operating within the laws I cannot conceive of a case where we would want to operate outside the law which exists at that particular time.

Mr. CHRÉTIEN: It is not a matter of law; it is a matter of spirit, you know.

The CHAIRMAN: Perhaps a specific example may help. Let us say you went to California and you were contemplating buying an established bank there.

Mr. HART: Mr. Chairman, we are in California now.

The CHAIRMAN: Say you went to another state.

Mr. HART: All right.

The CHAIRMAN: Let us say you went to see the treasurer of the State of Nevada—that is a neighbouring state—and said that you were contemplating buying the bank of Nevada, and the treasurer said: "At the moment nothing in our law prevents this but it is the intention of the administration to introduce legislation which would prevent this and to date it from a certain date, namely, today." What would you do?

Mr. MONTEITH: The answer would be very hypothetical, Mr. Chairman.

Mr. HART: It is very hypothetical. We have no thought of operating in the State of Nevada. I am not going to be facetious about this, but until we have a

case in point before us I think it is very difficult to say. There are many circumstances.

Mr. MONTEITH: You cannot get a free ruling out of the income tax department.

The CHAIRMAN: It would be a good idea if we could.

Mr. CHRÉTIEN: You are defending the position of an American bank. I am very surprised to hear you say that you were not aware of the situation at that time because it has been a subject of public discussion for years. You are speaking to us now just on the grounds that you respect the law and that is all. There is much more to it.

Mr. HART: Sir, I am not saying that I was not aware of what took place at about that time because it was certainly aired in the press. I was aware of what appeared in *Hansard* too, but I have seen no documents on this.

Mr. CHRÉTIEN: Sir, may I continue.

Mr. HART: The point I make is, as submitted in my brief, that there was no legal obstacle to the step taken by the Mercantile bank. I do not hold any brief for the Mercantile bank but this is a principle which is involved. I do not know to what extent they have made arrangements to acquire the shares of the Mercantile bank at that time, which were foreign owned. I do not know that; it is not my problem. The Mercantile bank was foreign owned when it was established in Canada and continued to be foreign owned, and I think they are changing the rules in the middle of the game just because the beneficial ownership changed from one country to another country.

The CHAIRMAN: I think in fairness we should give the floor to Mr. Monteith, who has been very patient.

Mr. MONTEITH: Mr. Chairman, I do not expect to be long. Despite the fact that you have read into the record a statement by the ex minister of finance, I claim there are two sides to every question.

The CHAIRMAN: I think you are quite right.

Mr. MONTEITH: The other side has not had an opportunity of putting forth its argument in this particular respect. I want only to say that I agree with Mr. Hart's presentation. I agree with the intent behind it, and I think we should not change rules in midstream.

Mr. Hart, because of various banks in Canada operating in several states of the United States, are you at all worried about possible retaliation by either the federal system in the United States or any particular state banking system? And have there been any signs whatsoever thus far that there could be this retaliation?

Mr. HART: Mr. Chairman, first of all, we are concerned about retaliation. I am sure that the members of this distinguished Committee are aware of the fact that Senator Javits has introduced a bill into the Senate in the United States which would impose very severe restrictions of a retaliatory nature against foreign banks operating in that country. I would like to add, however, that long before this ever came up on at least two occasions in speeches which I delivered before public audiences I attacked, in shorter terms of course because it was part



of another address, this section 75(2) (g) or whatever the number may have been at that time, because the intention of the government had been declared in the first bill to revise the Bank Act, but this was subsequently withdrawn when parliament disbanded. So I do not wish any member of the Committee to feel that I am taking this action now because we fear retaliation in the United States. I took this action long before any such retaliation was ever even thought about to my knowledge, because this has only been a very recent development.

Mr. MONTEITH: I asked, have there been any signs thus far. You have mentioned Senator Javits.

Mr. HART: Yes. I guess that covers it, Mr. Monteith.

Mr. MONTEITH: Mr. Chairman, that is all I have at the moment.

The CHAIRMAN: I should tell the Committee that I have been informed—and I could be wrong in this—that the Javits bill died on the Congressional equivalent of the order paper when Congress ended for their own recent elections.

Mr. MONTEITH: There is still an indication.

The CHAIRMAN: I am not saying that.

Mr. GRÉGOIRE: It might come back.

Mr. CHRÉTIEN: Senator Javits is from New York State and there is no Canadian bank operating there. There is only an agency, which is quite a different topic.

Mr. HART: I do not submit that it is a different topic at all. We are operating freely in New York state under New York state banking laws, with the one restriction which was in force at the time we established our operation down there and which we accepted. They have not, to my knowledge, changed the rules since.

The CHAIRMAN: I have the text of the Javits bill and Mr. Javits' introductory statement. It might be useful if I had the Clerk make copies of these and circulate them. It may be that the members of the Committee will feel that in addition to the possibility of retaliation Mr. Javits was concerned with the balance of payments problem in the United States and also the fact that there is no central federal control of entry of foreign banks. In his text, which I will leave to the consideration of the members of the Committee, he refers to the need to protect the national interest of the United States.

Mr. Monteith do you have further questions?

Mr. MONTEITH: Thank you; that is all I have at the moment.

*(Translation)*

Mr. CHRÉTIEN: Whether you be operating or not, the question remains the same, because if you were told, "Do not buy the shares of such and such a bank, or do not proceed with such a business transaction because it is not appropriate", would you accept the proposal made to you? Would you say, "Under the law, we will keep strictly to the letter of the law, and not to the spirit that is now current."

The CHAIRMAN: I will now give the floor to Mr. Laflamme, then to Mr. Cameron.

(English)

Mr. LAFLAMME: Mr. Chairman, I personally would like to congratulate the witness for his strong personal views on what he thinks is discrimination. However, I am not very convinced now that this is discrimination.

Mr. Hart, you did not deal with the main principle involved in clause 75, the question of Canadian banks operating in Canada not being pressed too much by foreign investments. There is quite a difference, in my view, when comparing Canadian investments with American investments in the United States. In my opinion, the Americans are so rich that they would not be too concerned about Canadian investments competing in the United States. But in Canada the situation is quite different. May I have your views on the main principle involved, the timing of this proposed legislation, which is a different thing.

Mr. HART: Mr. Chairman, I believe Mr. Laflamme is introducing the subject of foreign investment in Canada, not necessarily foreign control. Let us deal with it in two parts.

Mr. LAFLAMME: Foreign control of banks.

Mr. HART: Foreign control of banks?

Mr. LAFLAMME: Yes.

Mr. HART: I wanted to deal with the question of foreign capital coming in, but apparently that is not the question.

If the legislation now rules that there is to be a prohibition against any other foreign banks coming into Canada or even taking an equity position in a bank to be formed, or even an existing bank—and the rules are going to be laid down under the present Bank Act—all well and good. I still submit that in the case of this particular bank in question they operated fully under the rules of the game at that time, and therefore they deserve protection under the law because they operated, as I say, within the framework of the Bank Act. They were chartered as a chartered bank of Canada and could operate in the same way as any other chartered bank; and they have done so.

Mr. LAFLAMME: Mr. Hart, that was not my question. Regardless of the present situation of the Mercantile bank, what are your views on the actions of the government to put restrictions on foreign capital to keep them from perhaps gaining control of Canadian banks.

Mr. HART: You have introduced the subject of foreign capital, and although I would like to dwell on that I will not at this time.

So far as foreign capital coming in to attempt to control or take over an existing Canadian bank or to establish a new bank—and I think there are two questions there—I would like to put it this way. Banking, if I may say so, is an honourable profession, and if it is to the advantage of the country as a whole that a banking operation would be strengthened by having additional capital come in, even though it may be foreign owned, I submit that that is good for the country. I would far rather see a well-established and highly regarded foreign bank establish an operation in Canada than to have a group of individuals within Canada who never have been in the banking business before attempt to establish a banking operation. I think that the prestige and the strength of an institution built up over many, many years of operations is a very important factor. I would like to make that particular point.

The CHAIRMAN: If in 1817 when the merchants who wanted to start the Bank of Montreal, with no banking experience, had come forward would you have made the same response to them?

Mr. HART: I was not there in 1817, Mr. Chairman. I will say that a number of the individuals who formed the Bank of Montreal in 1817 came from Boston and already were versed in the banking business in the United States.

Mr. LAFLAMME: Mr. Hart, you made a very strong statement when you said that if the Mercantile bank had been bought by interests either from Britain or France such legislation would not have been enforced.

Mr. HART: Mr. Laflamme, this is rather hypothetical, but I have a suspicion that this might have happened. We have the case of Barclay's bank establishing a bank in Canada some years ago, which was subsequently taken over as you know by another Canadian institution. But it was established by a British bank.

Mr. LAFLAMME: Yes. Then you cautioned against the main view of the government putting something in the legislation which will protect Canadian banking interests.

Mr. HART: If it is the wisdom of parliament now that legislation should be enacted to prevent this from happening again, and if that is the wish of parliament, then we must abide by it. But I do not think that you can change the rules for an existing organization such as the Mercantile or any other bank which might have been involved, which was operating within the full provisions of the law of the Bank Act under which they received their charter.

Mr. GRÉGOIRE: Even if they were aware of this when they acquired the interests of the Mercantile bank?

Mr. HART: Mr. Grégoire, even if they were aware of it because—I go back to my brief—there was no legal obstacle to the step which they took and the new owners acted quite within their rights under existing law.

The CHAIRMAN: Mr. Hart, before recognizing Mr. Cameron I want to ask you about something that just occurred to me. Is what happened here, the minister of finance telling these people about the intentions of the government to change the law at a time when the law permitted conduct other than what was contemplated any different than the minister of finance getting up in the House of Commons and making his budget speech, which refers to tax changes, which would not be passed into law for weeks or months after the budget message was given, but yet would be retroactive to the date of the message?

Mr. HART: Tax legislation, thank goodness, in this country so far has not been retroactive.

The CHAIRMAN: Wait a minute, sir—

Mr. HART: The budget may be introduced, stating what the taxes are going to be or what changes in the act are going to be effective at a future date that everybody is aware of. But this was not discussed in Parliament at that time, as I recall.

The CHAIRMAN: I am trying to see if there is an analogy. Am I not correct that in many cases the tax changes mentioned are considered to go into effect at the moment the budget speech is given.

Mr. HART: Correct?



The CHAIRMAN: But at that moment there is no law calling for those changes; the law itself does not come into effect, in many cases, until months later and is retroactive. What the minister says in his budget speech is merely a comment in the house. Is this any different than what happened with the Mercantile situation, with the exception that it was done in the minister's office rather than in the House of Commons.

Mr. HART: Mr. Chairman, I am at a disadvantage, not being present when the conversation took place, although I know what is on the record. I must agree with what Mr. Monteith said. It does seem abundantly clear to me, and again I am speaking without certain knowledge so I should not say "abundantly clear" because I do not know at what stage negotiations had been reached between the parent institution, which subsequently became the parent institution of the Mercantile bank, and the previous Dutch owners or the owners at that time of the shares of the Mercantile bank. I am not aware of that and I find it very difficult to speak to this point. If they had gone to the extent where they had closed the deal with the Dutch owners of the Mercantile bank, had acquired the shares from the Dutch owners—and this again is hypothetical because I do not know what went on; I am not privy to that conversation at all and came up here as a matter of courtesy to tell the officials of the Government of Canada what they had undertaken, well, then, I still say they were operating within the law.

The CHAIRMAN: What if the conversation was exactly as described in the *Hansard* record.

Mr. MONTEITH: Mr. Chairman, on a point of order. This seems to me to be an inquisition against Mr. Hart rather than actually against the Mercantile bank. I submit that if we are going to continue in this vein and take the minister's statement as gospel, we must have before this Committee the officials of the Mercantile bank so that they can defend their own position.

The CHAIRMAN: The officials of the Mercantile bank, as you may be aware, are going to appear a week from today.

Mr. MONTEITH: I was not aware of that.

Mr. GRÉGOIRE: Will Mr. Walter Gordon appear too?

The CHAIRMAN: If the Committee wishes. It is up to the Committee to call anybody they wish Mr. Hart is here today. He is very frankly and very fairly putting forward some views, which are most useful to the Committee. As you may know, the Committee also has agreed to hear Mr. McLaughlin of the Royal Bank, though not necessarily on this subject, on Tuesday. Then, on Thursday, the official from the Mercantile bank are going to appear.

Mr. MONTEITH: Mr. Chairman, I was not aware of that. Was there any reason why I should be? The notices have not gone out yet for each day's program.

The CHAIRMAN: No, but this has been discussed at Committee meetings.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The list of witnesses was circularized to members of the Committee.

Mr. MONTEITH: It was discussed on November 24, Mr. Chairman, and I was not at that meeting.

Mr. HART: Mr. Chairman, I would like to make this point very strongly. I am not here to appeal on behalf of the Mercantile bank. They run their show; we, in

the Bank of Montreal, run our show. I am here to appeal on a point of principle irrespective of what bank might have been involved. I want to make myself quite clear on that point.

Mr. GRÉGOIRE: I have a supplementary question.

The CHAIRMAN: If Mr. Laflamme is finished, Mr. Cameron has the floor. It is up to him to yield to supplementary questions.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I am a little nervous about agreeing to Mr. Grégoire asking a supplementary question because he may go on for an hour. If it is a real short one I will give way to Mr. Grégoire.

Mr. GRÉGOIRE: It is a short one. Your remarks were on a principle you invoked. Would your intervention this morning be the result of the retaliation you fear in the United States.

Mr. HART: Definitely not, sir. As I mentioned early, I am on record in two addressess I made two years ago, when I appealed against this discriminatory legislation. This was long before there was any thought, as far as I know, of any retaliation in the United States.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Hart, as a banker, I presume you were aware that the Bank Act was due for its decennial revision in 1964.

Mr. HART: Yes, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would it be fair to suggest that on account of that imminent revision of the Bank Act, you would be keeping a very careful eye on statements of government officials on the possibility of revisions to the legislation?

Mr. HART: We know nothing of the legislation until we actually see the draft brief. We had no discussion prior to that, to my knowledge, with any government officials on what they intended to put into the draft bill. Our first knowledge is when we see the bill after it has been introduced in parliament.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I have not been suggesting that you had discussed this with the government, but I am suggesting that surely you were aware of the statement of the former minister of finance which the Chairman has read to this Committee.

Mr. HART: Yes, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): And you were aware that that statement did appear in *Hansard*, an official document of the House of Commons.

Mr. HART: Yes, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): So would I be unfair to suggest that perhaps you were a little disingenuous when you suggested you had seen no documents relating to this matter?

Mr. HART: No, I did not mean to imply that, sir. From what I understand there was one memorandum or perhaps more prepared of conversations that took place which I have not seen and, naturally, would not expect to see. But I was aware of what was on the record in *Hansard*.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then, in view of the imminent revision of the Bank Act and the statement of Mr. Walter Gordon, which certainly every member of the House of Commons accepted as a truthful report of the conversations he had had with the American interests who were then preparing to take over the Mercantile bank, would you not consider that this was a sufficient warning to dispose of your argument of discriminatory retroactive action because it was not possible for Mr. Gordon to embody that idea in legislation until the legislation came before parliament. But did he not give fair warning?

Mr. HART: Yes, sir; I must agree to that. As I say, I know what was on the official record, and I do not for one minute question the statement made by the former minister of finance. But even though he had issued this warning to the proposed purchasers—and I say “proposed” in quotes because I am not sure what state their negotiations had reached with the Dutch interests at the time they called on the minister of finance. I am not aware of that so I cannot speak truthfully to that point, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You mentioned your suspicion, that had these been interests of a different nationality that quite likely this legislation would not have come up. You mentioned also that you would like to embark on the question of foreign investment in Canada. As you are well aware, there is a wide debate going on in Canada right now on the danger of an increasing foreign ownership of our resources and our industries. Would your position be that there is no danger, that we have nothing to be concerned about, when such a large proportion of our economy is now in foreign hands.

Mr. HART: Is that your question, Mr. Cameron?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes.

Mr. HART: I submit there is no danger. I think we have to go back a bit, certainly, prior to the second world war, to the development which has taken place in this country since that time, and I do submit that if we had not created a climate—and thank goodness we did create such a climate—which enabled foreign capital to come into this country and help develop our tremendous natural resources, and brought along with that technical know-how in which we were not experienced, I think this country has benefited a very great deal from foreign capital, whether it came from the United States, Great Britain or other countries in Europe. If we can continue to have a climate which will attract good capital into this country and help to develop the growth of this country, I submit that is good for Canada. I think it would be a sorry day if the climate ever became such in this country that foreign capital no longer came in because I think that we Canadians as a whole would suffer as a result.

(Translation)

Mr. CHRÉTIEN: A supplementary question, with your permission, Mr. Chairman?

The CHAIRMAN: If Mr. Cameron will permit you?

Mr. CHRÉTIEN: Yes, he gives me permission, Mr. Chairman. Mr. Hart do you not find there is a difference between investment in general and investment in sectors that is important for our nation, as banks, radio, television and news-



papers. Do you not distinguish between these two types of foreign control over our economy?

(English)

Mr. HART: In dealing with foreign capital I was very conscious of the fact. I take as an example the development of the oil and gas industry in this great country of ours. I do not think it would have proceeded to the extent that it has without capital and technical know-how coming in to assist in its development. Now you are getting into other areas such as broadcasting and newspapers. I do not know that I am too well qualified to discuss that particular aspect of the topic. But if foreign investment coming into Canada is coming from groups who are well established, well regarded, people of high principle, people who have operated in their particular field for a long period of time and who have experience and know-how and are willing to invest in Canada for the benefit of Canadians generally, then I think it would be a sorry day if we slammed the door in their faces.

Mr. CHRÉTIEN: Yes, but you do not make any difference between the general investment and the specific areas that I mentioned, banking, radio and newspapers. You see no danger to the personality of our country if we leave these very sensitive fields in Canada to foreigners?

Mr. HART: I think we are straying a bit away from the revision of the Bank Act. I would answer your question in so far as banks are concerned. I would attempt to repeat what I said before, that if we have a well established foreign banking institution abroad—whether it is in the United States or wherever it may be—one that has prestige, one that is well regarded, I think it would be to our benefit if they came in and participated in the further growth of the Canadian economy.

The CHAIRMAN: What if they purchased an existing Canadian bank.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): That is the question I was just going to ask if I could continue.

The CHAIRMAN: Oh, I am sorry. We will take it as being asked by Mr. Cameron.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I was going to ask you, Mr. Hart, what your view would be if at some time in the future—if we did not pass this legislation to which you take some exception, although not as strong an exception as you do to that regarding the Mercantile bank—there was a determined and successful attempt on the part of a foreign financial institution to take over one or more of the existing chartered banks in Canada?

Mr. HART: Mr. Cameron, the question is a bit hypothetical because it would take a very vast amount of money, I think, to take over one of the major chartered banks of Canada. I cannot conceive of any well established, well operated, banking institution or financial institution abroad that would attempt such an exercise. I think they would prefer to come in and establish a supplementary or a new operation rather than attempt to take over an existing operation. This, of course, is all hypothetical. I cannot really answer this.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But what is not hypothetical of course is the fact that the world's most powerful and most wealthy

financial institutions are in the United States. Does this not have some bearing on our attitude toward representatives of that extremely powerful, almost overwhelming, economy moving into the operation of one of our financial institutions in this country?

Mr. HART: Mr. Cameron, first of all I am a dyed-in-the-wool Canadian. I am not holding any brief for the United States or any foreign country; do not get me wrong in that. I do, in answer to your good question, submit that it is in the interest of Canada—and we must always keep that in mind—to have a strong partner come in to help with further development in our country, that is to our advantage.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Could you explain to the Committee how this would be to the benefit of Canada. I presume that a foreign bank coming in and establishing itself would operate on the same basis as the existing banks?

Mr. HART: Under a charter?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, it would have a charter. Is it not correct that their operations would be based on their ability to attract the savings of the Canadian people in deposits.

Mr. HART: That is correct.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then in what way would you advance the interests of Canada by having those deposits divided again in another way?

Mr. HART: I am trying to make my point, Mr. Cameron, on the benefit to the economy as a whole. It is not just a matter of a new chartered bank being established, gathering up deposits or making inroads on deposits held by existing banks or other institutions at the present time. If we have a strong organization that comes in here, operating in the international field, then I think that would be a tremendous help to Canada in furthering our export trade and other matters because I am sure we are very conscious in Canada of the importance of export trade to this country. Anything that helps to develop that, as a case in a point, I think is to our benefit.

The CHAIRMAN: You mean the Bank of Montreal could not expand to pick up that challenge?

Mr. HART: We are attempting to grow with the country and play our part in the growth of the country at all times. But we are a Canadian institution even though we do operate certain establishments abroad such as I have mentioned, and there are quite a few others too. We cannot handle all the foreign business; perhaps all the Canadian banks together cannot handle the foreign business because a lot of it comes from outside. If we have a partner or somebody who comes in who is able to bring further expertise and facilitate the growth of exports and trade generally in this country then, I submit that is to our advantage.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Hart, are you telling us that in your view the Canadian banking institutions are not capable of serving the interests of Canada.

Mr. HART: No, sir, I am not saying that at all. I am speaking from the standpoint of Canadian institutions operating in Canada. When you get into the foreign field you do have to have co-operation with other institutions abroad in countries where the Canadian banks are not operating. Naturally, there are many countries in which we do not operate. Therefore, we rely on banking correspondents and other institutions to assist in the promotion of trade to the benefit of their country and to the benefit of Canada. We cannot do it all ourselves; there is a matter of co-operation which enters in here.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Is this not rather a different element that you are introducing now? No one is suggesting that you should not co-operate with financial institutions in other parts of the world; you obviously have to. Is this not rather a different proposition than suggesting that because of the incapacity, I gather in expertise and possibly resources of the Canadian banking fraternity it would be desirable to have a foreign bank establish itself in Canada.

Mr. HART: Mr. Cameron. I am afraid we are arguing at cross-purposes. I am not saying that the Canadian banking system is not doing its job. I, by no means, intend to imply that whatsoever because I think we are doing a good job in this country. But when you get into the international field, co-operation is necessary, and certainly we obtain that. If a foreign institution wishes to establish in Canada, be it banking or whatever field it may be, which is going to be to the benefit of Canada, then I think that is good for the country if this is going to help, say, promotion of further trade between the respective countries involved.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Now, just to define some of our terms, You speak of co-operation in one breath and in the next you speak in terms of establishing a bank in Canada. Have you experienced any difficulty in getting co-operation from foreign financial institutions in your world trading operations?

Mr. HART: No, sir, I would not say that we have encountered any difficulty. I think, sir, you introduced the matter of a foreign bank coming in for the purposes of this discussion. I was just trying to imply that if it is a well established, well recognized, well run institution which is willing to come into Canada and take a state in this country, then I think that we certainly would look for benefits from that because this is expanding further the international operations. We of course are vitally interested because of the importance of export trade to Canada in broadening the scope of operations in that particular field.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Hart, you have already told me that so far as you know you have not encountered any difficulty in getting co-operation from foreign financial institutions. Are you suggesting that a bank established by foreign interest in Canada would have better co-operation throughout the world?

Mr. HART: I would not say it is a matter of better co-operation, Mr. Cameron, no. I would say that if a foreign institution comes in here they obviously are taking somewhat of a stake in this country and that we should benefit because, presumably, with their international operations elsewhere, they would have more interest in developing trade between Canada and other countries involved because they have a stake in this country.



Mr. FULTON: You mean more interest than they would without a stake in the country?

Mr. HART: No, sir, I do not think more interest. If they are operating in Canada under Canadian law then I think if they are willing to come in and throw their lot in here—

Mr. FULTON: My interjection was because I felt your answer was open to interpretation and that you were saying that this foreign bank would have more interest in developing trade than the Canadian banks.

Mr. HART: Oh, no, sir. I did not mean to imply that.

Mr. FULTON: It is one of the implications that has been taken by Mr. Cameron.

Mr. HART: I stand corrected then. I did not mean to imply that at all.

Mr. FULTON: You meant they would have more interest in developing it than they would if they were not in Canada.

Mr. HART: If they were not here; that is correct, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): More interest in developing trade between Canada and the rest of the world?

Mr. HART: Sir, that is correct.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would they have more interest than the present Canadian banking fraternity?

Mr. HART: No, I would not say so at all.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Hart, I must say I find it rather difficult to understand your position because it does seem to imply that you find some shortcomings in our Canadian banking institutions, that they are not capable—

Mr. HART: No; I by no means intend to imply that whatsoever, Mr. Cameron.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You repeatedly come back and tell us that a foreign bank with foreign connections would be in a better position to expand our trade than one without it. Are you telling us that you do not have the foreign connections?

Mr. HART: No, sir. I am not saying that they would be in a better position to expand our trade. I am saying that in considering the matter as a whole this is another group which would be in a position to assist in expanding our trade. I cannot say that they are going to do a better job. I think we in the Canadian banking system can be justifiably proud of the way it has grown up and the part we have played in the development and growth of the economy of the country. But anything that is going to further the growth or further that development, if it is in the interest of Canada, I think we should be willing to accept.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Does it not boil down to this, that they merely divide the existing opportunities and resources in Canada that are now at the disposal of the present existing Canadian financial institutions. You are no further ahead, are you? Are they going to have extra resources?

Mr. HART: Mr. Cameron, I am looking at it from the standpoint of a foreign institution coming in and naturally, bringing in new capital to a certain extent too. We do not deal in foreign trade in Canadian dollars, as you may know, it is largely in United States dollars and sterling in Canada. Our Canadian dollars, so far as foreign trade is concerned, are of no use except to the extent that they are used to purchase foreign exchange to pay for imports.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): This is a very important use.

Mr. HART: It is a very important use but that is imports. I am talking really about developing our export trade, and if we can get additional institutions who are willing to come in, as part of their operation, to further that export trade, then I submit it is good for the country.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I think that is all for now, Mr. Chairman.

The CHAIRMAN: I now recognize Mr. Leboe, followed by Mr. Gregoire.

Mr. LEBOE: Mr. Chairman, I am interested, first of all in the principle that was enunciated by Mr. Hart. I follow you to a point but I fail to follow you to the nth degree. I think there is always a point in any possession, any deed or title, where we come to the matter of the good of the community. I think you admit this. I am not saying that I am on your side or on anybody's side because that is not the point. I want to deal particularly with this matter. Suppose we find ourselves in a position in a community where a man has a clear title to a piece of property and that it is in the interest of the community that man divest himself of that property, and he says: "This is my home; it is my castle; I built here with every intention of spending all my life here, and I am not interested in selling it at any price." The thing to do then is to expropriate. In other words, we change the rules in the middle of the game by using expropriation. I think, whether or not we go ahead on this particular section, that the principle which you have enunciated is broken down, on the basis of the principle of expropriation to the benefit of the community. Am I not right?

Mr. HART: I must admit that I am not a lawyer.

Mr. LEBOE: Well, I am not either, so we are on equal footing.

The CHAIRMAN: Then this discussion, can be carried on quite untrammelled by the detailed knowledge of the law.

Mr. FULTON: I am unhappy about one aspect of Mr. Leboe's statement.

Mr. LEBOE: Well, please let the witness answer, and then you can make your remarks afterwards. I would like the witness to explain his position because of the principle that he was enunciating so strongly, that it should never be varied by law, even if it was to the better interest of Canadians.

Mr. HART: Mr. Leboe, there certainly is a matter of principle involved here, leaving expropriation aside for the moment, if I may. The point I make is that when you operate within the law, as I have submitted in my brief, then the entity involved is deserving of the full right of protection of that law. When you get into the expropriation of a piece of land, I think we are in a little different area.

Mr. LEBOE: I said the man's home is his castle. He was operating within the law when he built his home.

Mr. HART: But, Mr. Leboe, if we are talking about expropriating a bank or any institution in Canada, I think we are going to have one awful fight.

Mr. LEBOE: I am talking about changing the rules in the middle of the game.

Mr. FULTON: Mr. Chairman, is not the expropriation law that Mr. Leboe speaks of on the statute books of Canada in every province right now?

Mr. LEBOE: You are on the wrong track. We are not talking about the expropriation law; we are talking about the changing of the rules in the middle of the game for the benefit of the community.

Mr. HART: Well, you are not changing the rules if the law already exists, Mr. Leboe.

Mr. LEBOE: So far as the individual is concerned, just the same as the Mercantile bank, you certainly are changing the law because the individual has no knowledge that eventually there will be a highway or something else going through his land. He has knowledge of that. He may have been there for 50 years and all of a sudden there is a change in the world which makes it necessary to change the course of events. I am not saying that I am against the Mercantile bank or anything at this particular moment; I am not putting myself on any side. But surely we are in the position that with the passage of time we have to change. As I understand your position, Mr. Hart, the principle of not changing the rules in the middle of the game should be in perpetuity. I cannot agree.

Mr. HART: I only apply it to the case in point. You have introduced a question, Mr. Leboe, of expropriation of property.

Mr. LEBOE: That is only an example.

Mr. HART: You used that example though.

Mr. LEBOE: I can cite other ones as well.

Mr. HART: No doubt you can, sir. There are laws on the books now covering expropriation. The individual may not be aware of that, but when he is faced with it I am sure that he scurries around to get a good lawyer to help him out. I do not want to be facetious but you may be aware that down in New York City—I think it is in Queens—Macy's were putting up a big department store and there was a little old lady who owned a small property on the corner which they could not acquire. Nobody attempted to expropriate it. She is still there. They had to build around it.

The CHAIRMAN: Macy's is a privately-owned body.

Mr. HART: That is correct.

Mr. LEBOE: This only strengthens the position that I am taking. This is not necessarily for the good of the community; this is for the good of Macy's. This only strengthens the very argument that I have been making.

You did mention the inflow of capital. If the total amount of resources being developed is Canadian resources, and if the end result is that we have total Canadian labour applied to those resources in order to develop them, is there any reason why we cannot supply the capital for it from Canada without going outside when we are using our own resources and our own labour.



Mr. HART: Sir, I think we could not have begun to generate the capital required in Canada for the tremendous developments that have taken place in the last 10 to 20 years. I do not think there was enough risk capital around in Canada to do this.

Mr. LEBOE: This has not answered my question. You are around the corner on me already. I am saying to you that if all the resources involved are Canadian resources and the total amount of applied labour is Canadian labour then why in Heaven's name can we not supply the capital from within Canada, because money does not grow on bushes.

Mr. HART: That is correct.

Mr. LEBOE: We have a banking system set up, with the Bank of Canada and its governor as the main valve, as it were, to handle the expansion of the money supply, with a certain amount of direction, as he has testified before this Committee. If these are Canadian resources and the total amount of labour that is being applied to these resources is Canadian, are our financial institutions in Canada not capable, with the co-operation of the Bank of Canada, especially now under the new legislation, of generating this amount of capital in Canada, with the resources of Canada backing up that capital.

Mr. HART: Mr. Leboe, I think you are getting into the area of voluntary policy, and fiscal policy too for that matter. In so far as monetary policy is concerned the chartered banks in Canada have no say in it.

The CHAIRMAN: If I may interrupt here, gentlemen, we have already decided that we would deal first with the topic raised by the witness in his brief. After we have exhausted that, within some reasonable limits, then we will go on to discuss other topics.

Mr. LEBOE: Mr. Chairman I must object because one of the main arguments that was used by the witness was the introduction of new capital.

The CHAIRMAN: If you are relating your questions to the issue, raised by the witness' brief, then that is fine.

Mr. LEBOE: Certainly, substituting Canadian resources, with Canadian labour applied, for foreign capital is relevant in this particular case.

The CHAIRMAN: So far as it is related to the specific issue raised by Mr. Hart's brief.

Mr. LEBOE: I have raised the issue and I think that somewhere along the line the banking institution, particularly since it has been brought into this argument so forcefully as far as foreign capital is concerned, will have to be dealt with further in the Committee.

The CHAIRMAN: I am not saying it cannot be dealt with; I am just suggesting unless you are in a position to relate this particular type of question to the treatment of the proposed legislation of foreign owned or foreign controlled banks in Canada, then you defer it until we have exhausted the topic.

Mr. LEBOE: Although I will defer it, it is related because it is foreign capital, which has to do with that question. I will pass for now.

The CHAIRMAN: Mr. Leboe, do you have any further questions at this point?

(Translation)

I now recognize Mr. Grégoire.

Mr. GRÉGOIRE: Mr. Hart, your main objection is to 75 (g) (2). This section mentions only those banks where more than 25 per cent of the shares are held by one person—whether he be a resident or a non-resident. Is the Mercantile Bank only in that position with more than 25 per cent shares held by any non-resident?

(English)

Mr. HART: Is the Mercantile bank the only one in that position? Mr. Grégoire, I believe that is the case.

(Translation)

Mr. GRÉGOIRE: What about the Bank of Montreal. Do you not have shareholders who hold more than 25 per cent of the shares?

(English)

Mr. HART: No, we do not. Over 86 per cent of our shares are owned in Canada.

(Translation)

Mr. GRÉGOIRE: So, the Mercantile Bank alone is involved. You have other reserves in this clause. The liability should not be more than twenty times the authorized capital stock. Do you know if any other chartered banks have total liabilities of more than twenty times the authorized capital stock?

(English)

Mr. HART: Yes, they all have, Mr. Grégoire.

(Translation)

Mr. GRÉGOIRE: However, in the case of the Mercantile Bank, it is the only bank whose shareholders are non-residents in which the liabilities are twenty times the capital stock.

(English)

Mr. HART: Well, this is what is introduced in the legislation.

(Translation)

Mr. GRÉGOIRE: In fact, however, the Mercantile Bank of Canada is the only chartered bank in Canada belonging to non-residents and whose total liabilities exceed twenty times the authorized capital stock.

(English)

Mr. HART: Right.

(Translation)

Mr. GRÉGOIRE: Under the circumstances, then, since we are dealing here with the banks where the investors are non-residents, do you not think that it would be security for the Canadian depositors, altogether apart from the case of the Mercantile Bank of Canada—only as a matter of principle—for all foreign institutions or individuals, being the majority shareholder in a chartered bank, to be limited in their operations by a clause such as this?

(English)

Mr. HART: No. If you are speaking of the other chartered banks apart from the Mercantile I do not think this question—

Mr. GRÉGOIRE: I am speaking about any individual in the United States who would like to take control and start a new chartered bank. Should we put that clause into the Bank Act for the security of Canadian depositors?

Mr. HART: No. I would not think that with a new chartered bank established in Canada there is any need to put in this security in the form in which you stated.

Mr. GRÉGOIRE: If it is from non-residents?

Mr. HART: Mr. Grégoire, the section covering the 25 per cent control is another matter; it is not related to the amount of liabilities in relation to the capital of that particular institution.

Mr. GRÉGOIRE: Would it be a matter of good security for Canadian depositors to accept any foreign control without at least a minimum of security like that provided by clause 75 of the bill?

Mr. HART: As I have tried to point out clause 75 is very restrictive and discriminatory against one chartered bank at the present time. Mr. Grégoire, I do not think it has anything to do with the security of the Canadian depositors because the chartered banks after all operate within the law of the country. We have been around for a long, long time and I think that Canadians generally have faith in the chartered banks in Canada and the way they have been operating. I do not think anyone is going to lose sleep overnight for fear that they are not going to be able to draw their money out of a chartered bank the following morning.

(Translation)

Mr. GRÉGOIRE: If the Mercantile Bank of Canada were not involved by this clause 75, would you object anyhow to this clause?

(English)

Mr. HART: I would not see any necessity for the clause, Mr. Grégoire, because I think this has stemmed from an attempt to embody legislation that is restrictive and discriminatory against one institution. I think if this had never arisen—and again this is hypothetical—there would not have been such a clause introduced for existing Canadian chartered banks because there would be a need for it.

(Translation)

Mr. GRÉGOIRE: Now, do you believe that the statement made by the former Minister of Finance, Mr. Walter Gordon, actually constituted a sufficient warning given to the people who bought out the Mercantile Bank of Canada? Was it sufficient warning? Did they know what was going to come about?

(English)

Mr. HART: As I say, I do not quarrel with the statement produced in *Hansard*. I do not say that it is wrong and I do not question it in any respect. As to the matter of sufficient warning I think we must know, and I certainly do not know, at what stage the negotiation had been reached between the Dutch interests and the United States interests who were asking to acquire them or



who had arranged to acquire them. Maybe they had already bought the shares. I do not know.

Mr. CHRÉTIEN: But, Mr. Hart, in the minister's statement at that time it was stated that no firm commitments had been made with them. According to what Mr. Gordon said it had been mentioned by the First National City Bank that no firm commitments were made with the Dutch interests at that time.

Mr. HART: Well, at this time I am not aware. I submit, Mr. Chairman, that this is something that can only be brought out when the witnesses on behalf of the Mercantile bank are here. I am not in a position to argue this point.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The Mercantile bank did not produce a statement?

Mr. HART: They may have. I do not know what their submission is at all, Mr. Cameron.

(*Translation*)

Mr. GRÉGOIRE: Mr. Chairman, this is my last question. Could we say that your position could be changed should other witnesses come here to confirm the warning previously given by the then Minister of Finance to the purchasers of the Mercantile Bank of Canada. Could your position change? Would your brief be other than it is? Would you be ready to amend it if you received confirmation by the former Minister of Finance of that warning?

(*English*)

Mr. HART: Well, sir, I can only go back to the statement I made before, that to my knowledge there was no legal obstacle to what was done in this case, where the ownership of the Mercantile bank changed hands, because it was a foreign owned operation in the first place. When it received its charter it was 100 per cent foreign owned by Dutch interests.

Mr. GRÉGOIRE: Was there not a clear warning by the then Minister of Finance that something close to a legal obstacle existed.

Mr. HART: I would not say it was a legal obstacle, Mr. Grégoire.

Mr. GRÉGOIRE: I did not call it a legal obstacle.

Mr. HART: You said close to a legal obstacle. I would not say so because there was no law on the books preventing this from being done. I am not in a position to state what went on at these discussions—and I do not suppose anybody is around this table. In deference to the gentlemen over here, I do not know what stage they had reached in negotiations for the purchase of these shares.

(*Translation*)

Mr. GRÉGOIRE: That is not my question, Mr. Hart. My question is this. Supposing we receive confirmation of formal advice being given by the Minister of Finance, would you be ready to amend your brief?

(*English*)

Mr. HART: No, I would not be ready to amend my brief, Mr. Grégoire, because I submit what was done at that time was quite legal under existing law.

(Translation)

Mr. GRÉGOIRE: Even though the Minister of Finance clearly indicated at the time to the parties involved in that transaction that a revision of the Bank Act was due in 1964, and further, that there would be a clause in this revision to the effect that we have been discussing to-day? Was that not sufficient warning, was that not such as to give all the information required to the people involved?

(English)

Mr. HART: Well, it may have been a warning, Mr. Grégoire, but it was still not law.

Mr. GRÉGOIRE: Was not the warning by the then minister of finance that they were going to amend the Bank Act soon sufficient?

(Translation)

The CHAIRMAN: I suggest that it is nearly one o'clock and you could continue your questions after the noon recess.

Mr. CHRÉTIEN: I have only one question.

Mr. GRÉGOIRE: I will put my questions this afternoon.

Mr. CHRÉTIEN: Mr. Hart, do you share the views expressed in the following statements, that Clause 75, 2(d), might constitute discrimination. But do you not feel it constitutes discrimination against all banks because at the present time, no Canadian citizens may acquire more than 25 per cent of the shares of any bank in Canada?

(English)

—if more than 25 per cent of the issued shares are held by any one resident or non-resident.

Mr. HART: I do not think it is discrimination against the chartered banks as such.

Mr. CHRÉTIEN: No, but it is discrimination against any Canadian citizen who wants to own 50 per cent of the shares of any bank.

(Translation)

The CHAIRMAN: We are going to have a continual exchange of questions and we might end our discussion at this point, with every consideration for our colleague, Mr. Grégoire.

(English)

Mr. Hart, perhaps we should let you think about your answer to that one. I will declare the meeting recessed until 3.45 p.m.

#### AFTERNOON SITTING

The CHAIRMAN: Gentlemen, I think we are ready to resume the meeting which was recessed this morning, and Mr. Grégoire will have the floor.

Before resuming I would like to inform the committee that our research staff has prepared two memoranda for Mr. Clermont, one headed Bank Service

Charges and the other headed Instruments Eligible for Rediscount at Federal Reserve Banks, that is to say, reserve banks in the United States. Mr. Clermont has indicated to me that he would be quite willing to have these same documents made available to the other members of the committee. Therefore, I am going to ask our clerk to have them duplicated and circulated and after you have had a chance to take a look at them I would be prepared to accept a motion, which would not appropriate at this time for obvious reasons, to have them added to our minutes in the usual manner.

Mr. LEBOE: I just want to express my appreciation to Mr. Clermont for doing that.

The CHAIRMAN: The approach we have been following, of course, is that where a member has some special work done for him by our research staff to assist him in preparing his own questions, it would be up to the member to make the material available in its entire and complete form to the other members of the committee. However, where I as chairman ask for material for the committee, or a member asks that the same material be made available to the entire committee, it will automatically be distributed or made available, as, for example, the table prepared by Mr. Baribeau on N.H.A. mortgage lending by banks. As to the two memoranda, the one on service charges prepared by Miss Prentis and the one on rediscounting at federal reserve banks by Mr. Baribeau, I have asked our clerk to distribute them in the usual way as soon as possible.

I will now give Mr. Grégoire the floor.

Mr. GRÉGOIRE: Mr. Chairman, I wonder if first I could be permitted to ask one or two factual questions of Mr. Elderkin, as Inspector General of Banks, for clarification of the problem we are now studying.

The CHAIRMAN: Well, I had better hear the questions and we will see.

Mr. GRÉGOIRE: Mr. Elderkin, were you present in the office of the then Minister of Finance, Mr. Gordon, when representatives of the First National City Bank came to Ottawa for discussions with Mr. Gordon regarding the transactions of the Mercantile Bank of Canada?

Mr. ELDERKIN: Yes.

Mr. GRÉGOIRE: Can you remember who were present from the First National City Bank at this meeting?

Mr. ELDERKIN: Mr. Rockefeller and Mr. McFadden.

Mr. GRÉGOIRE: Was it not understood at that time, and was it not plainly stated, that no definite commitments had been concluded concerning this transaction of the Mercantile Bank of Canada at the time of that meeting?

Mr. ELDERKIN: Yes, I think the memorandum that the former Minister of Finance tabled in the House contained that statement.

Mr. GRÉGOIRE: It was admitted at that meeting, was it?

Mr. ELDERKIN: I said that.

Mr. GRÉGOIRE: Is it not a fact that at that same meeting a very precise and concrete warning was given by the then Minister of Finance to the effect that section 75 or something to that effect would be included in the new bank act?



Mr. ELDERKIN: No, the warning was only that there might be legislation restricting foreign-owned banks.

Mr. GRÉGOIRE: There was a warning, then, that there might be some restrictions in the new bank act concerning that problem?

Mr. ELDERKIN: There was no indication of what type it would be.

The CHAIRMAN: You mean there was no indication specifically referring to the type of restriction?

Mr. ELDERKIN: The type of restriction that would be imposed.

The CHAIRMAN: Were the government's views clearly expressed on what their intentions were at that time?

Mr. ELDERKIN: I would say there was no indication of the type of restriction. It simply said if there was legislation restricting the growth of foreign-owned banks that he, the minister, would not consider after the warning that it was retroactive.

Mr. GRÉGOIRE: So then the warning did not include that precise fact?

Mr. ELDERKIN: That is right.

Mr. GRÉGOIRE: And the minister said that if it included this precise fact it would not be retroactive?

Mr. ELDERKIN: I think you have misunderstood. The minister said that if there was legislation restricting the growth of a foreign-owned bank he would not consider it retroactive after warning was then given. The Minister said that if Parliament later imposed restrictive legislation on foreign-owned banks that he, the Minister, would not consider that retroactive considering the warning he was given at that time.

The CHAIRMAN: You mean if the legislation dated back to cover—

Mr. ELDERKIN: That is right.

The CHAIRMAN: —the situation discussed with the minister by the gentlemen from the First National City Bank, it would not be considered retroactive because a warning had been given in the course of that discussion?

Mr. ELDERKIN: That is right.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): A warning that he considered to be tantamount to the legislation.

Mr. ELDERKIN: Well, Mr. Cameron, he did not express what the legislation might be, he simply said if there were restrictions imposed.

Mr. GRÉGOIRE: Is there not a kind of—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Did not his statement that he would not consider it to be retroactive mean that he considered that his warning was of such a definite nature that it would—

The CHAIRMAN: He would not consider that it would not be retroactive.

Mr. GRÉGOIRE: We are mixed up now. Can you clarify the matter?

Mr. ELDERKIN: What he said was that he would not consider it as being retroactive.

Mr. GRÉGOIRE: He would not consider it as being—

Mr. ELDERKIN: —retroactive, because they had been warned at the time that there would likely be legislation.

Mr. GRÉGOIRE: So it would apply to them. It was a fair warning, then. Is it not also a fact that the representative of the First National City Bank at that moment said that if the transaction was done after this warning it would be at their own risk?

Mr. ELDERKIN: I believe the words were “at their own peril”.

The CHAIRMAN: Mr. Grégoire, I think—

Mr. GRÉGOIRE: Mr. Chairman, that was my last question.

The CHAIRMAN: Yes. I think this subject matter is certainly relevant to our study of this legislation, particularly this area, but in view of the fact that Mr. Hart himself was not, as far as I am aware, participating in these meetings that a detailed inquiry into what happened there, beyond the statement formally given in the House by the Minister of Finance and some limited background so we understand what the background was to the minister's statement, would, I think, be better put off until the individuals specifically concerned with this issue are before us next week.

Mr. GRÉGOIRE: Well, Mr. Chairman, I asked those questions because this morning Mr. Hart said that he was not personally aware what stage the negotiations had reached between the Dutch and the Americans into the transaction at the moment of the warning. So now we have an answer from Mr. Elderkin that there was no definite commitment at that time between the American and the Dutch people. Now, we know that Mr. Elderkin was there. We also know that there was a fair warning given at that meeting to these people from the First National City Bank, and we also know that they admitted that if such a transaction was undertaken it was something that was done at their own risk.

Now, in view of these facts from someone who was present, do you think—when nothing definite was done—it is still discrimination when they knew in advance what was coming on and when they admitted themselves that it was at their own risk if they were still going along with the transaction? Do you still think it is discrimination?

Mr. G. ARNOLD HART (*General Manager, Bank of Montreal*): Yes, Mr. Grégoire, I still consider it discrimination. I would like to clear up one point, if I may by directing a question to the Inspector-General. In the earlier part of his statement I believe he said that someone—maybe the Minister of Finance, I do not know—said that there might be legislation introduced. Later on he said there would be legislation introduced. Which is correct?

Mr. ELDERKIN: If I said there would be legislation introduced I did not intend to say so. In the memorandum which was tabled in the House of Commons the minister said that normally it would be unfair to apply retroactively any legislation restrictions on control of banks by non-residents, but since the First National City Bank were now aware of the Government's views about the possibility of their acquiring the shares of Mercantile, the government would not consider that they would be entitled to exemption from any legislation in respect of foreign ownership that might be enacted in the future.

The CHAIRMAN: What is the date of that memorandum?

Mr. ELDERKIN: July 18. It is the one that the former Minister of Finance tabled in the House.

The CHAIRMAN: What was the date of the meeting?

Mr. ELDERKIN: July 18, 1963.

Mr. GRÉGOIRE: I think it was in October of 1963 that the transaction was concluded after the meeting. Now, in view of that fact and in view of the fact that the people from the First National City Bank were fully aware of the possibility of new legislation, and in view of the fact that they admitted it was at their own risk, would you still consider it discrimination?

Mr. HART: Mr. Chairman, I find myself in a rather awkward position here, not having been present at the meeting. Naturally I would not be there. Secondly, I think these are questions which should be directed to representatives of the Mercantile Bank or the First National City Bank when they appear. I am hardly in a position to discuss this.

Mr. GRÉGOIRE: Yes, but you are the one who took the position—

Mr. HART: That is right. Let me add this, Mr. Grégoire. I still feel that it is discriminatory, and I also question whether it was good principle to issue a warning such as that to an institution that action was going to be taken subsequently which would be directed against that institution. Is it a fact that members of the government will go out and warn anybody in advance of what is likely to be taken by way of legislative action against any particular entity or corporation? Is this good practice?

Mr. GRÉGOIRE: It is good practice to advise those that will be affected by such legislation. For example, when the B.C. Bank was in front of the Senate or the committee here they were advised in a speech from the Minister of Finance that governments would not be entitled to buy shares. So, it was before Bill No C-222 was presented to the House. They were advised and the Mercantile Bank were advised, because they were the only ones involved in such a problem.

Mr. HART: Mr. Grégoire, you speak of the Bank of British Columbia, which was not then and is still not in existence. I am speaking of a case of a corporate entity which was in existence and which was operating under the laws of the country at that particular moment.

Mr. GRÉGOIRE: Yes, but the people from the First National City Bank had not yet acquired it.

Mr. HART: I cannot argue with you on this, Mr. Grégoire, because I do not know. I must accept the statement that has been presented here. I think this is a question which should be directed to the representatives of the Mercantile Bank when they appear. I am not in a position to argue their case and I am not arguing their case. I am arguing a matter of principle.

(Translation)

The CHAIRMAN: I think your questioning time is finished. Have you another question to put, Mr. Laflamme? Are you going to begin a new round of questioning?



(English)

Mr. LAFLAMME: I had some questions to ask. Did you have any comments you wanted to make before I begin?

The CHAIRMAN: I wonder if it would not be useful at this point, in view of Mr. Hart's reference in his brief to the operations of his bank in New York and elsewhere, if the committee might find it useful to find out a little more about the extent and method of operation. Mr. Hart—

Mr. GRÉGOIRE: Mr. Chairman, before you go into that, just as a matter of clarification to instruct the whole committee, can we find out from Mr. Hart what is his understanding of discrimination? Perhaps the word "discrimination"—in French it is la discrimination—does not have the same meaning in English and that is why I have difficulty following it. May we have your understanding of discrimination?

The CHAIRMAN: I think we may be reaching this situation, that in spite of your vigorous questions Mr. Hart may not be willing to yield to your point of view or the point of view of others on the committee. Certainly that is something that can happen with any witness appearing before us. It may be that the committee will feel that he has sustained his position in the course of questioning, and if that is so it is up to the committee to decide. But I do not think we can expect—and this may happen with any witness—that he will necessarily be willing to shift his position entirely in response to the questioning of someone as vigorous and as intrepid as yourself. Therefore I think we have to recognize there may be some reasonable limits—I am not saying we have reached them—to pursuing any particular line of inquiry.

Mr. GRÉGOIRE: It is just whether it has the same meaning in both languages, Mr. Chairman.

The CHAIRMAN: Well, are you in a position to define your use of the term "discrimination"?

Mr. HART: I would be glad to attempt to do so, Mr. Chairman, in simple terms. The point I make is that the Mercantile Bank in this particular case was operating under the laws of the country, having been given a charter and become a chartered bank of Canada along with all the other banks and then legislation is introduced which singles them out under this section 75(2)(g) for special treatment which does not apply to all the other banks. This I call discrimination.

Mr. LEBOE: On that point, Mr. Chairman, I do not think it is quite correct to say they were singled out. I think it would be more correct to say they were the only ones affected.

Mr. HART: I will accept that, Mr. Leboe.

Mr. LEBOE: Thank you.

The CHAIRMAN: I think perhaps it would be more convenient to defer any questions I had in mind on the operation of agencies and to permit Mr. Laflamme and yourself, followed by Mr. Cameron, to continue with questions more directly relevant to the area we are in now with respect to Mr. Hart's brief.

(Translation)

Perhaps you have questions to put, Mr. Laflamme?

(English)

Mr. LAFLAMME: I would first like to ask some questions of Mr. Elderkin. In Canadian history is this the first time the whole interest of a Canadian chartered bank has been bought by foreign capital?

Mr. ELDERKIN: No, Barclays Bank (Canada) was entirely owned by foreign capital, British capital.

Mr. LAFLAMME: What bank was that?

Mr. ELDERKIN: Barclays Bank (Canada).

Mr. LAFLAMME: Barclays Banks?

Mr. ELDERKIN: Yes.

Mr. LAFLAMME: When was it in existence?

Mr. ELDERKIN: It was incorporated in 1929 and it was merged with the Imperial Bank of Canada in 1956, I believe.

Mr. HART: For the record may I state that Barclays Bank in the United Kingdom did not buy a Canadian bank. They established a new bank in which they owned all the shares. They did not buy an existing bank, they started a new bank.

Mr. LAFLAMME: This is the only reference you have regarding this, but you never had a situation where foreign interests have completely bought a Canadian chartered bank?

The CHAIRMAN: In order to avoid some misconception, who controlled the Mercantile Bank before the First National City Bank?

Mr. ELDERKIN: I was about to say, Mr. Chairman, the Mercantile Bank was set up as a fully controlled foreign bank when it was incorporated. The ownership was transferred later to another foreign ownership.

Mr. LAFLAMME: Then, Mr. Hart, except for the retroactivity which will apply in this bill regarding the Mercantile Bank, would you have the same or different comments to make regarding this law from those you have made this morning?

Mr. HART: Just to clarify this, Mr. Laflamme, did you say accepting or with the exception?

Mr. LAFLAMME: With the exception of this retroactivity applying to the Mercantile Bank, would you have the same views as those you made to members of the committee this morning?

Mr. HART: If I follow your question correctly, Mr. Laflamme, it is a principle I am arguing here, not just the Mercantile Bank. Now, you say if this should arise again? Is that your question?

Mr. LAFLAMME: Suppose this bill would not apply to all Canadian chartered banks, would you have the same complaint to make as the one you have made?

Mr. HART: If it applies to only one I submit it is discriminatory; that is, a bank already established. The Bank Act covers all chartered banks. They do not write one act for the Bank of Montreal and another act for the Banque Canadienne National. This applies to all chartered banks.

Mr. LAFLAMME: This morning in your statement you used the word "retroactivity", which was the main effect of the Mercantile Bank, what was discrimination to the Mercantile Bank, but without the application of retroactivity in this bill would you have the same comments to make?

Mr. HART: Retroactivity did come into the discussion this morning, but my brief was based on discrimination against one institution which was operating under the laws of the country at the time this change of ownership took place.

Mr. LAFLAMME: Perhaps I will ask the translator to deal with it.

*Translation*

Supposing, Mr. Hart, that the law would apply only to future banks, would you have the same comments to make, regarding this application of a 25 percent maximum interest for any bank any foreign interests might want to set up in Canada?

*(English)*

Mr. HART: I think I understand your question now, Mr. Laflamme. If the law applied to all banks in future, well then, I would not argue against that as long as all banks are treated the same. My point here is that there has been discrimination against one bank which was operating within the law. Does that answer your question?

Mr. LAFLAMME: Yes.

The CHAIRMAN: Are you suggesting, sir, that an entity or an individual in Canada is entitled to insist that the law which existed at the time of its entry into business continue to apply to it throughout its existence no matter what the changed circumstances may be?

Mr. HART: No. I think the point I am trying to make, Mr. Chairman, is that the law should apply equally to all entities operating within the jurisdiction under which they operate or within the law.

The CHAIRMAN: Yes.

Mr. HART: But that they should not single out one institution for special legislation, in effect, which does not apply to everybody.

Mr. LEBOE: Mr. Chairman, I would like to raise that same objection to singling out.

Mr. HART: I say "single out" because it happened to be the only one at the time, Mr. Leboe.

The CHAIRMAN: Perhaps we should clarify this. You will agree with me that the Mercantile is not referred to by name in the legislation?

Mr. HART: That is right.

The CHAIRMAN: We agree on that. And you would also agree that if any other bank in Canada got into the same situation this section would apply to it as well?

Mr. HART: I am not quite sure that I follow the question, Mr. Chairman. I am afraid I have lost myself.



The CHAIRMAN: Let me put it another way. If this law is adopted by Parliament—

Mr. HART: Yes.

The CHAIRMAN: —would it be possible for the Bank of America to come in and do something which the Mercantile, or the people controlling, it, would no longer be allowed to do?

Mr. HART: If the law as proposed is adopted by Parliament, well then, no other foreign bank could come in and do what the owners of the Mercantile Bank have done because there was no law at that time which prevented them from doing what was accomplished.

The CHAIRMAN: Except to the extent that the warning given by the Minister of Finance had some significance.

Mr. HART: Yes, but it was only a warning, it was not law and, as a matter of principle, should such warning have been given to one corporation like that?

The CHAIRMAN: Would you not have had a—

Mr. CHRÉTIEN: We often have guide-lines in many things, in matters of inequality, and so on, but most of the good citizens will abide by that.

The CHAIRMAN: If I may be permitted to continue.

Mr. GRÉGOIRE: It is Mr. Laflamme's turn for questioning.

The CHAIRMAN: Mr. Laflamme, I thought you had concluded.

Mr. LAFLAMME: No, I had not.

The CHAIRMAN: Oh, I am sorry.

Mr. LAFLAMME: No, you continue if you have another question.

The CHAIRMAN: What would you have said had the warning not been given?

Mr. HART: We are getting into a rather hypothetical area. If the warning had not been given perhaps this situation which we have at the moment might not have arisen in quite the same way. If the ownership of the Mercantile Bank had changed from Dutch to that of another nationality, and there was nothing in the law to prevent this being done and no warning had been given, I cannot quite follow why they would have proceeded other than they did.

The CHAIRMAN: I want to return to the question I began to ask you this morning, if Mr. Laflamme would permit me. I wonder if you could distinguish between what was done in this case and what is done every year with respect to the budget. I want to repeat the explanation I gave. At a certain point the Minister of Finance gets up in the House of Commons and delivers his budget speech. He says in his speech that the government is proposing certain tax changes, most of which—and I think Mr. Cameron will agree with me, as he is his party's financial critic who replies to the Minister of Finance—are deemed to go into effect at the very moment the speech is given. The law implementing these proposals is not presented to Parliament nor is it passed into formal effect until some months after the budget speech. Now, at the moment he gives the speech, strictly speaking, the law has not been changed. Would you say that somebody who did something that would not have been permitted once the law

was formally passed into regular effect, and which would then be dated back retroactively to the date of the speech, really have any complaint?

Mr. HART: Let me put it this way, Mr. Chairman. If the Minister of Finance in his budget address says that a certain tax, personal, corporate, or whatever it may be, is going to be changed effective the day on which he makes his budget speech, but that in fact the law is not proclaimed until some months later, as I believe you put it—

The CHAIRMAN: It is not merely not proclaimed, it is not even entered in Parliament.

Mr. HART: All right, I am sorry, I used the wrong term there. It is not enacted. It does not become law until some months later. Well, the individual or corporation concerned who is paying taxes will continue to pay taxes at the rate applicable at the time or even prior to the time the Minister of Finance made his pronouncement in his budget speech. The taxpayer does not immediately start paying higher taxes until the law is passed.

The CHAIRMAN: He is liable for them.

Mr. HART: That is right, too, but he is still a good citizen if he pays taxes at the old rate.

The CHAIRMAN: In fact—and I think Mr. Cameron may be able to tell us something about this—the government begins to collect, for example, higher rates of sales tax forthwith.

Mr. GRÉGOIRE: Immediately with the speech. It is not yet a law, but it is collected immediately.

The CHAIRMAN: Now, could you tell us really what is the difference between the two situations, except for the fact that the Minister of Finance, with respect to the Mercantile Bank, made his comments in private in his office, and with respect to the budget speech he makes his comments in the House of Commons?

Mr. HART: I think the difference is this, Mr. Chairman, that the Minister of Finance, when he makes his budget speech, directs it to all Canadians. He does not single out one firm or one individual and say, "You are going to pay higher taxes from this date". It applies right across the board.

Mr. LEBOE: Mr. Chairman, I think—

Mr. HART: If I may just complete this, Mr. Leboe, I think in this particular case there was discrimination because—I must not say single out, Mr. Leboe—it applied to only one corporate entity, which at that time was operating within the law and it still is.

Mr. LEBOE: With Mr. Laflamme's permission I would like to ask you this question. Would you not agree that all foreign interests—this is what we are dealing with—are treated the same under this legislation? We are dealing with foreign interests here and this is the question.

Mr. HART: Yes, with the exception of section 75(2)(g), which happens to apply to one entity at the present time, but if the law is passed it certainly applies to all foreign interests.

Mr. LEBOE: So there really is no discrimination, is there?

Mr. HART: Well, I think there is, Mr. Leboe, because the foreign interest at which this section 75(2)(g) is aimed was operating within the law and still is.

Mr. LEBOE: It happens to apply to these, but the discrimination that you are speaking of surely does not exist because it is applying to all foreign interests.

Mr. HART: When the law is passed.

Mr. LEBOE: That is right, so there cannot be any discrimination, then, can there? Surely not.

Mr. HART: I feel there is, Mr. Leboe.

The CHAIRMAN: Mr. Hart, if I might return to my budget analogy, and then we will give the floor back to Mr. Laflamme, the fellow who refuses to pay the higher rate of sales tax is, in a sense, also operating within the law as it exists at the moment the budget message is given.

Mr. HART: But as a good corporate citizen presumably he would pay the sales tax, I will agree to that.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Any corporate citizen will pay it; he is going to pay it anyway.

Mr. HART: Yes.

The CHAIRMAN: So you would agree, with respect to the budget message, that any citizen who did not take into account the tax changes that he knew would apply from that date would not really be able to blame anybody but himself for the consequences.

Mr. HART: That is true but, Mr. Chairman, any legislation introduced or any budget address, if we are using that analogy, applies to everybody in Canada to which the new tax applies.

Mr. GRÉGOIRE: The law will apply to everybody.

Mr. HART: Once the law is passed, yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It only applies to people in certain categories.

Mr. HART: When I say everybody I mean certain people are affected in different ways, but I think you know what I mean, Mr. Cameron.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): If there happened to be only one in Canada in that position, then would you say that was discriminatory?

Mr. HART: I certainly would.

The CHAIRMAN: If we wanted to pass such a law.

Mr. HART: If they passed legislation discriminating against one individual.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No, not against one individual but against any individual in that particular category. On this occasion there happened to be only one. Would you say that was discriminatory?

Mr. HART: I submit that it is discriminatory.

The CHAIRMAN: Just a moment, please. In other words, if the government passed a law dealing with telephones and there was only the Bell Telephone Company operating in this field, by your definition this would be discriminatory?



Mr. HART: Yes, I think I must agree to that because they would single out one corporation for special legislation.

The CHAIRMAN: In other words, by your term, sir, the government should never be able to pass a law dealing with telephones?

Mr. HART: We are getting pretty hypothetical because there happens to be more than one telephone company.

The CHAIRMAN: I might point out to you in passing, sir, that when we are talking about proposed legislation and proposed policy everything we say is hypothetical.

Mr. HART: Yes.

The CHAIRMAN: With all due respect to you, sir, if you want to attempt to limit questions on the basis that they are hypothetical our discussions here today will be severely limited.

Mr. HART: Mr. Chairman, I am not trying to limit anything at all. All I am trying to say is that when a budget is introduced in Parliament it is a precise budget, it deals with various aspects of the taxation of the economy, but a warning, such as was given in the office of the Minister of Finance, is not to me in the same category at all.

Mr. CHRÉTIEN: If one of the men who was there at that moment said, "I will operate this transaction at my own risk", is this not, in your opinion, an admission of an awareness of the situation?

Mr. HART: Mr. Chrétien, I think it is a little unfair, if I may put it this way, to question me—

(Translation)

Mr. CHRÉTIEN: It is a hypothetical question, once again.

(English)

I was not there.

Mr. GRÉGOIRE: Mr. Elderkin was there.

The CHAIRMAN: I think in all fairness to Mr. Hart we should not really attempt to put before him in too great detail the circumstances of this particular meeting. I think we can sketch it in broad outline based on the *Hansard* record and the documents tabled in the House, but to attempt to go beyond that do not I think would be fair to Mr. Hart.

(Translation)

Mr. COMTOIS: Could I put a question, please, to Mr. Hart?

The CHAIRMAN: Yes, to tell you the truth I thought that Mr. Laflamme had finished his round of questioning, it is why I began myself to make an inquiry of the sort. I believe to keep more or less in order it would be advisable to ask Mr. Laflamme, first of all, whether he has finished his line of questioning.

Mr. LAFLAMME: I have already said that I had not finished.

The CHAIRMAN: He said that he has not finished his line of questioning. If you want to put a supplementary question, we will have to ask whether he will

yield so that you may put your question. Mr. Laflamme should perhaps finish. If I remember correctly I did not follow his questions too closely.

(English)

Mr. LAFLAMME: Well, I do not mind at all. I am ready to ask Mr. Hart a few questions. I must say, Mr. Chairman, that I am not very much impressed if those people who wanted to buy the interests of that bank were or were not advised by the minister. Personally I go further than that; I think it implies the full capacity of the Canadian government to establish legislation which will protect and keep in sight the full control of this particular institution, which is a bank, because I think when the Canadian government decides to establish limits under which foreign capital may have interests in Canadian chartered banks I think it has established its own capacity of forming policies. Personally I do not recall any foreign government consulting Canada before establishing any financial policy within that government. I am not very much impressed if those people were or were not advised by the minister, even if I think it is a factor, when they talk about discrimination or a question of retroactivity. This was the main topic under which I wanted to ask my questions earlier. If, as you suspect, this legislation would not apply to the Mercantile Bank, would you have the same comments to make in view of the full capacity that the Canadian government must have to establish legislation in which it can control those particular institutions which are chartered banks, because it is not the same thing to have foreign capital invested in industry and to have foreign capital invested in banks. I would like to have your full comments on that.

Mr. HART: Well, Mr. Laflamme, if this situation with respect to the Mercantile Bank had not arisen at all.

Mr. LAFLAMME: Yes.

Mr. HART: We had never heard of it before.

Mr. LAFLAMME: Yes.

Mr. HART: And the Canadian government decides that in the bill now presented some action should be taken to ensure against the eventuality of, say, one of the chartered banks, or any or all of the chartered banks, coming under foreign control, then I think we are in a different set of circumstances because the legislation then introduced would apply to all banks equally and there would be no discrimination. This is assuming that the Mercantile situation had never arisen.

Mr. LAFLAMME: Yes.

Mr. HART: But in view of the fact the Mercantile Bank is a chartered bank of Canada, and therefore operates within the law exactly the same as all other chartered banks operating under the Bank Act, and legislation has been introduced by virtue of the fact they are the only one to which it applies,—again not using the term “singled out”—then I think there is discrimination against that one particular institution.

Mr. LAFLAMME: But it was the first time that such a thing happened in Canadian banking history, if I may say so.

Mr. HART: I believe that is correct, Mr. Laflamme, as the Inspector General testified. The bank in question was foreign-owned from the outset, but this is the

first time to my knowledge that the beneficial ownership has changed from that of Dutch nationality to United States nationality or nationality of any other country, whatever it might have been.

Mr. LAFLAMME: Thank you.

Mr. HART: The Barclays Bank case we mentioned, of course, was established by British capital and was taken over by a Canadian institution, the Imperial Bank of Canada, which is a different set of circumstances.

Mr. LAFLAMME: Yes, indeed. Thank you.

The CHAIRMAN: I think Mr. Cameron is next, followed by Mr. Johnston and Mr. Comtois.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Chairman, I want to ask Mr. Hart some questions. I hope you will not think that I am stealing the questions you were going to ask because I had written down these questions before you intimated that you intended to ask them. However I should be very glad to yield to you any time you think I am doing it inadequately.

The CHAIRMAN: If it turns out, quite independently of any contact, that our minds have seized upon similar questions, I consider it somewhat of a compliment that my mind should follow lines similar to those of the chief financial critic of the New Democratic Party.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): All right, Mr. Chairman, you win. Mr. Hart, I notice that in your brief on page 4 you make mention of the fact that the Bank of Montreal has operated in the international field longer than any other Canadian bank, and so doing it has invariably behaved as a good corporate citizen, and so on. Now, the next sentence reads as follows:

More important, we believe that the extension of our facilities into other countries has played a constructive part in facilitating the development of Canada's international, commercial and financial contacts.

Now, I was wondering, Mr. Hart, if I could ask you to describe for us—I may tell you I know nothing about this, I am completely ignorant—the type of transactions that your New York agency performs, for instance?

Mr. HART: To be as brief as possible, Mr. Cameron, our New York agency operates as an agency, and not in the same context as any other American bank down there within the federal reserve system, with the restriction I mentioned this morning. We are in a position down there where we do a very substantial securities business on behalf of clients of the bank. Our business down there is really set up to assist Canadian clients of the bank. We are not down there to compete with the other United States banks established in New York city. This is not the object of the exercise. But we do provide facilities to clients in Canada, whether they be individuals or corporate entities, and when they are dealing with the Bank of Montreal in Canada we can look after requirements which they might need in the New York market, whether this is to help them in trade matters, to develop contacts for them down there or to assist in the financing of these transactions when they come up. There are really a whole host of services which we can provide, and without going into a very lengthy explanation I hope that answers your question. It is purely an operation to aid and assist primarily our Canadian clients. Now, of course, we do have a lot of international clients,



not in New York but abroad, in Europe, who deal through our New York agency, and also in South America, Latin America, and so on, who deal through that agency too. Primarily our chief aim is to look after and serve the requirements of Canadian customers to the greatest extent possible.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then it would be correct to say that your operations there could be considered as being primarily advantageous to Canada?

Mr. HART: Yes, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would it also be true to say they are advantageous to the American economy? Do you do anything there that an American institution could not do as well for the American economy?

Mr. HART: I think perhaps the only area in which we are performing a service to the American economy is where we employ surplus United States funds not otherwise required at any particular moment of time in the call loan market in New York. I gather you know how the call loan market functions.

The CHAIRMAN: Perhaps you could describe it for us briefly.

Mr. HART: The call loan market really deals in loans to brokers and dealers for the purpose of carrying securities. It is the same as we operate here in Canada but this is in United States dollars. These loans are subject to call, they are highly liquid, well secured, and it is a means of employing surplus United States dollars for a short period of time. This money keeps turning over.

The CHAIRMAN: If I may interrupt Mr. Cameron here, as he already invited me to do before beginning, would I be correct in saying the agencies of Canadian banks operating in the call loan field in New York finance about 70 per cent or more of the loans to brokers and dealers for purchase of securities on the New York market?

Mr. HART: I do not think I can tell you what the percentage is, I think it might be a little high, but I would have to get that figure for you, Mr. Chairman. I do want to make this point. This is only a means of employing surplus funds not otherwise required, so that the money can be put out at interest on short term loans in the call loan market. Now, if a Canadian client comes along and says he wants to borrow X dollars from the Bank of Montreal, then if necessary we can call one or more of these loans and provide the dollars for the Canadian borrower. It is not an attempt on our part to look after American requirements, because this could be done by the United States banks. This is merely a means of employing our surplus requirements at any given moment so the money is not lying idle.

The CHAIRMAN: I understand that but, if Mr. Cameron will permit me to continue, the fact is that the brokers and dealers in securities in the New York market must consider your service and those of other agencies in this regard to be very useful?

Mr. HART: I should think they would, Mr. Chairman, yes.

The CHAIRMAN: And while you would not agree with my figure of 70 per cent, you would agree that a very high proportion of the call loans for the purposes you have outlined are made by agencies of Canadian banks?

Mr. HART: That is correct.

The CHAIRMAN: It would seem to me, therefore, that it would be detrimental to the dealers in this market if this source of operation was not available to them.

Mr. HART: We are not so concerned about whether it is detrimental to the dealers in that particular market as we are concerned with employing surplus funds at a time when they are not otherwise required, but they are funds on call, so that when they are required we can get them immediately to use for other purposes.

The CHAIRMAN: Oh yes, I recognize that, and I want to make clear I am not attempting to suggest you are using funds that might be better employed elsewhere.

Mr. HART: No.

The CHAIRMAN: But what I am trying to find out, sir,—and you have in effect said this—is that you had your fellow agency operations are performing a very valuable service for an important part of the New York security market, there is no question of that?

Mr. HART: Yes, that is right.

The CHAIRMAN: So it would appear, therefore, that if there was some attempt at retaliation by legislation on the part of the United States government, some sizeable group of fairly important American citizens would be very upset about it.

Mr. HART: I assume that would be the case, yes.

The CHAIRMAN: It might well follow, then, that these people would resist very strongly any attempt, by way of possible retaliation for any action the Canadian Parliament might take, to limit your very useful operations in the New York market?

Mr. HART: Well, Mr. Chairman, I do not know to what extent or how strong that voice might be from the call loan market in the matter of retaliation. I submit there would probably be many other factors involved. They might be one group that would be effective, I do not know. We do not know what the nature of the retaliation might be at this particular time, although we have had an indication in the bill which I mentioned this morning.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): If I could proceed, Mr. Chairman—

The CHAIRMAN: Go ahead.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): To the extent to which there would be a similar opportunity in Canada for an American institution—not a branch of an American bank—it could be performed by a similar agency, could it not?

Mr. HART: Yes, I quite agree, Mr. Cameron. I think that reciprocity is important. Here the Canadian banks, to the extent that they operate agencies in New York,—not all of them but most of them do—I think we could hardly say that we should not permit a foreign bank to come in and establish an agency in Canada on the same basis. In other words, operate on the same basis that we operate in New York, as an example.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): In your opinion would it be likely that an American bank would be interested in doing so?

Mr. HART: I would think so, yes. After all, the American banks, even at this point in time, do a fair amount of business in Canada. We, in turn, do a fair amount of business in the United States.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I gathered at present there are no agencies of American banks in Canada, is this right?

Mr. HART: Not of American banks.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Of American banks, that is what I mean. Although it has not been illegal for them to enter Canada up to this point, has it? Has it been illegal?

Mr. HART: To come in and operate an agency? Well, there is no legislation covering agency operations of which I am aware.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Perhaps Mr. Elderkin could answer my question.

Mr. ELDERKIN: I would answer it the same way. There is no legislation which would permit them to operate in Canada.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But there is no legislation to prohibit them from operating?

Mr. ELDERKIN: They could not use the words bank, banker or banking.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I see. But they could use the word "agency", could they not?

Mr. ELDERKIN: As long as they did not specify of whom they were the agent.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Oh. All right.

Mr. FULTON: That has been done.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Now, with regard to your San Francisco branch, Mr. Hart, is it able to do anything for the benefit of the American economy that an American bank could not do?

Mr. HART: No, I would not say so, Mr. Cameron. It is not a branch, if I may correct the record here, it is a wholly-owned subsidiary of the Bank of Montreal in California. It is operating under state law and therefore, as I mentioned this morning, they can do exactly what any other bank under California law can do. There are no restrictions on us. I think perhaps the one advantage is that there are a lot of firms in California who have operations in Canada or who are dealing with Canada, or who are exporting to Canada or perhaps importing from Canada, and we have broader facilities than perhaps a bank which operates solely in California and does not have an operation in Canada. In other words, we could facilitate them more readily by looking after their requirements in California and looking after their requirements in Canada.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would not an American bank be able to establish the same connections?

Mr. HART: They would have to do it through a correspondent, which might be any one of the chartered banks with whom they happened to have a corre-



spondent relationship, but we feel we have a little more intimate relationship this way because we are dealing with a client in California who also has interests in Canada and therefore he only has to deal with one bank.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Do you have a branch in the United Kingdom?

Mr. HART: Yes, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): That is a branch?

Mr. HART: That is a branch, sir, yes. We have two branches, in fact, in London.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): In London. Are those branches able to do anything for the benefit of the United Kingdom economy that a British bank could not do?

Mr. HART: I think probably in the same context that I answered your question about California, where a company in the United Kingdom also is interested in exporting to Canada or importing from Canada. We can look after their requirements in the United Kingdom and, because of their interests in Canada, they only have to deal with us, or any other bank in the same position. We can facilitate the transaction, we feel, more readily than a bank which did not have a connection in Canada.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Is it not the usual procedure to have a correspondent bank?

Mr. HART: Oh yes, I think, frankly, every bank must have correspondent banks around the world.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): All around the world.

Mr. HART: Let us take a case in point. Suppose we have a customer in the United Kingdom who is operating a subsidiary in Canada and wishes to arrange for a loan in Canada. This can be arranged for them through our London office, although the loan is going to be on the books of some branch in Canada because they would be dealing in Canadian dollars and not in sterling, as they would in the London market. So we can facilitate the transaction for them there by closing the deal, if I can put it that way, in the United Kingdom and putting it on the books of the branch concerned in Canada, but the loan is made in Canada to a company operating in Canada.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Hart, concerning this anxiety you appear to have—and I think it is a perfectly justifiable anxiety, your brief suggests that the Canadian government's action with regard to the Mercantile Bank may cause retaliatory action against the operations of your bank and any other Canadian bank in the United States, would you consider that that danger would be obviated if provision were made for the establishment of agencies of American banks in Canada?

Mr. HART: I am afraid, Mr. Cameron, I cannot speak for the United States government in this. There have certainly been suggestions in the press that merely allowing agencies to come into Canada is not going to cure this problem with respect to the bank which we are discussing today, but this I do not know. This is hearsay. I certainly have had no discussions with officials in Washington. These are statements made in the press or views expressed by various people or

groups of people in the United States. But it all gets back to reciprocity, and I think that if the Canadian banks enjoy the privileges we do in the United States, that for the benefit of the international picture and for the benefit of Canada as a whole, as applying totally to the banking system, it is a good thing to have other banks take an interest or take a stake in this country, even though it is only in the form of an agency, so they can facilitate operations further.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You cited, as a sign of the possibility of retaliation, the bill presented by Senator Javits, although I understand from what the Chairman said it died on the order paper of the United States Senate, is that right?

The CHAIRMAN: That is the information I have.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Even so, I note, in reading Mr. Javits' remarks about it, that all his bill would do would provide for federal control and licencing of foreign banks because he feels, and I think this is the important thing, the state authorities do not have enough concern with regard to the international implications of having foreign banks in the United States.

The CHAIRMAN: The national implications as well.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The national implications too. But it does not threaten to chase you out of New York, it only means that you would have to have approval from the federal authorities as well as the State of New York.

Mr. HART: May I read this section—I think you have the Javits' bill before you—which I think is applicable.

If at any time—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Which section is that?

Mr. HART: I am looking at page 7 of a copy of this Javit's bill, Mr. Cameron.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): What section is it?

Mr. HART: It is under Compliance with Rules, section (b) starting at line 15 on the sheet I have before me. Well, you have not got the same copy but there is a heading, "(b) Compliance with Rules". Is that in your copy?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Is there a section number?

Mr. HART: There is no section number. This is Bill No. S-3765. I do not know where it would be in your copy.

The CHAIRMAN: It is the same bill. We have an extract from the Congressional record and you have a photostat.

Mr. CHRETIEN: It is on the second page of our copy at the middle of the page.

The CHAIRMAN: Oh yes, it is under the heading of Authority of Comptroller.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Oh yes, authority of comptroller. I see it, yes.

Mr. HART: The excerpt reads:

If at any time, the foreign government under whose laws the parent bank of the agency, branch, or controlled subsidiary was organized, changes its laws or regulations affecting United States banks operating

thereunder (directly or through subsidiaries) the Comptroller of the Currency shall have authority to impose the same conditions upon the foreign banking corporation or its branch, agency or controlled subsidiary operating within—

—any state. This is retaliation.

The CHAIRMAN: But this is prospective, not obligatory.

Mr. HART: Well, this is not yet law.

The CHAIRMAN: I would just point out to you, sir, that as I read this it gives the comptroller of the currency authority but it does not impose upon him the obligation to take any such steps.

Mr. FULTON: Have you never heard those endless discussions in the House about the words "shall" and "will" as applied to the Governor in Council?

The CHAIRMAN: We hope they have not gotten into the same ones in the United States.

Mr. HART: I guess we are into semantics, but it is certainly clear, "shall have authority to impose the same conditions". Now, I am not in any position to say whether he would exercise that authority or not.

The CHAIRMAN: No.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I think, Mr. Hart, you have told us enough to indicate that you perform a very useful function in the New York market and I think the very fact that no American banks have established agencies of the same sort in Canada would indicate that this is a function which is a factor in New York's position as the chief money market of the world. Would it not appear to you extremely unlikely that they would dispense with an agency that was serving their purposes as well as the purposes of Canadian clients?

Mr. HART: I think, Mr. Cameron, you may have a point there, but let me attempt to answer it in this way. I think the New York market—and let me include the London market too, the two major financial centres of the world—achieved that position of prominence because they did permit foreign banks to come in and operate in those markets.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Do you not think there is some connection also with the fact that the American economy is the largest and most highly developed in the world?

Mr. HART: Well, it was not always. The United Kingdom—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): And New York was not the major money market in the world at that time.

Mr. HART: That is right, but I think the operations in the international sphere of foreign banks in these two markets, New York and London, have made a great contribution to the growth and importance of those markets. Who is to say that the situation might not eventually come about in Canada, if we made it possible for foreign banks to come in and operate even on an agency basis in Canada, where we would be expanding our operations in the international field for the benefit of Canada. In other words, we would be establishing a good money market here, such as they have in New York and London, in the international field.



Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Are you seriously contending, Mr. Hart, that until the Canadian economy approaches the degree of magnitude of the American economy that we are not going to establish an international money market of the same degree?

Mr. HART: No, I am merely saying, Mr. Cameron, that if foreign banks, regardless of what country they may come from, establish operations in Canada, it is conceivable that in time the importance of Canada as a money market would come about, the same as it has in New York and in London. The only point I am trying to make is that I think having these foreign banks in those markets has been of assistance in the growth of those markets.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I wonder, perhaps, if there is not some confusion between cause and effect here, and the existence of the foreign agencies in New York was a result of the predominant position of the American economy in the world?

Mr. HART: Mr. Cameron, if we go back 107 years, this is when the Bank of Montreal established the first foreign bank agency in New York. We were the first of any banks around the world to establish a foreign bank agency in New York and certainly New York did not have the prominence then that it has now. I am not saying we led the way or we were the means of bringing this about, but nevertheless we did operate an agency in the city of New York. Why was that done? It was to facilitate trade between Canada and the United States. If my memory serves me correctly, I think the Bank of Montreal was instrumental in floating the first United States dollar issue by a Canadian province in the New York market. Now, I am not saying this would not have been done if we had not been there, but because we were there we were able to facilitate the transaction. This happened many, many years ago.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Even at that period the relative importance of Montreal and New York was probably about the same as it is today, was it not?

Mr. HART: Oh, Mr. Cameron, I do not know whether I can say yes or no to that.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You had the same situation as far as Canada was concerned vis-a-vis the United States that obtains today, and your predecessors were particularly prescient in realizing that this was a good place to get into.

Mr. HART: You mean when the Bank of Montreal was established?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes.

Mr. HART: Oh, yes. Of course, there was a lot of trade then between Boston and Montreal, not New York primarily, it was largely Boston.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes.

The CHAIRMAN: Mr. Johnston and then Mr. Comtois.

Mr. JOHNSTON: Thank you, Mr. Chairman. It is suggested, Mr. Hart, that the Mercantile Bank could disregard monetary policy laid down by the Bank of Canada. You have been very concerned about an institution operating within the law. This is a somewhat slightly different matter, but would you care to com-

ment on the possibility of a foreign-owned bank being able to disregard monetary policy?

Mr. HART: I think the Mercantile Bank would always operate as a good citizen in this country and would not disregard monetary policy as laid down by the Governor of the Bank of Canada. I think this may be a question you should direct to the Mercantile Bank, but I would strongly suspect that they would co-operate to the hilt, as all other chartered banks do because they are a chartered bank.

Mr. JOHNSTON: Yes, but on the other hand the possibility is there because of their direct access to extra funds which other chartered banks would not have at their disposal?

Mr. HART: Well, access to what funds, Mr. Johnston? They are operating in Canada as a chartered bank and the money supply is controlled by the Bank of Canada. I do not think they can wave a magic wand and get more Canadian dollars than any other chartered bank can within the orbit of monetary policy.

Mr. JOHNSTON: Suppose between November 30, 1963 and April 30, 1965, for example, the Mercantile assets jumped 50 per cent, and partly because of the infusion of outside funds. There are sources of outside funds available to a foreign-owned bank.

Mr. HART: Yes, this could certainly happen, that they might be willing to bring in funds from, say, the United States or other countries and convert them into Canadian dollars. I do not think this is something that is to the detriment of Canada as a whole if they are providing funds, but once they come in in the form of Canadian dollars they are part of the money supply. They cannot, as I say, wave a magic wand and create a little bloc of Canadian dollars all by themselves which are not under the jurisdiction of the central bank.

Mr. JOHNSTON: The call loan market in New York which the Chairman questioned you about at some length, and in which the interest of the Canadian banks seems to be a little larger than simply to serve the interests of Canadian business in New York, as you more or less suggested, has been described as lucrative. Would you care to comment as to how lucrative?

Mr. HART: First of all, Mr. Johnston, the operations in the call loan market are not done to facilitate Canadian interests in Canada because this is a different exercise completely. We only use the call loan market for the employment of short term funds at interest so that the money is not lying idle, because we pay interest on the funds we have collected through deposits and therefore we hope to employ those funds at a reasonable margin of profit which will make the exercise profitable. The profits are not exorbitant, I can assure you. You see, you are operating in a very sophisticated market with adequate liquid security behind your loans and therefore the rate of interest charged is very low in relation to what a borrower might pay for a commercial loan. So that the spread between what you are paying for your deposits and what you are getting for the loans on the call loan market might be very narrow indeed. It might be  $\frac{1}{8}$  of 1 per cent or  $\frac{1}{4}$  of 1 per cent.

Mr. JOHNSTON: The money used in this operation would be entirely within the New York banking picture. It would not, at any time involve a transfer of funds from your bank operation here in Canada?



Mr. HART: No. It is not to the detriment of Canada at all, oh, no. These are United States dollars with which we are operating in the New York market.

The CHAIRMAN: It is very helpful, at least, to the New York financial market?

Mr. HART: Oh yes, but you must understand it is also helpful to us, Mr. Chairman, because we are employing funds on a short term basis in a highly liquid loan in order to earn a reasonable rate of return on funds on which we are, perhaps, paying interest to the depositor. These are United States dollars; we do not withdraw Canadian dollars from Canada to employ them in the United States market. In other words, we do not buy United States dollars to employ them in the United States market.

Mr. JOHNSTON: It sounds like a possibility now. I know you have just said that you do not do this, but it is theoretically possible.

Mr. HART: Theoretically possible, but I think rather impractical because we could probably earn a better return using the dollars in Canada than converting them into United States dollars, taking an exchange risk and getting a very small rate of return in the United States.

Mr. JOHNSTON: Would you comment on the suggestion that this legislation that is before us now would set an international precedent that might be copied by other countries that had American-owned banks operating within them?

Mr. HART: I think it could be, Mr. Johnston. I think if Canada earns the bad reputation of acting in a discriminatory manner that not only might there be retaliation in the country of our neighbours below the border, but in other countries where Canadian banks are operating. We are not only in the United States, as you know.

Mr. JOHNSTON: To go back to my original question, you described the operation as discriminatory. Might it not also be described as taking steps to protect the monetary interests of the nation?

Mr. HART: Yes, if the law is passed on this basis to protect, and again I go back to a comment I made earlier, that if this particular situation had not arisen and it was deemed by Parliament that action should be taken against an eventuality, something that has not arisen but something which might arise in the future and it applied to everybody, well, I do not think we could really quarrel with it. There is no discrimination there.

Mr. JOHNSTON: Thank you.

*(Translation)*

The CHAIRMAN: Mr. Comtois?

Mr. COMTOIS: Mr. Chairman, I would like to make a point with regard to the principle at issue in clause 75 2-g. The principle at issue is "limiting control of Canadian chartered banks by foreign interests". That is the basic principle, the principle which is at issue, and even if this principle seems to be discriminatory in regard to banks, I think that the contrary would be in favour of this bank because it was advised it should not take control of the Mercantile Bank before the purchase of that bank. Those people did run this risk by control in the Mercantile Bank and they will have to accept the fact, I think, that control is



going to be imposed on the share of foreign capital in Canadian chartered banks, because that is the principle which is at issue, the degree of foreign control over chartered banks. Could I have Mr. Hart's comments on that?

*(English)*

Mr. HART: I think there are two sides to this question, Mr. Comtois. First of all, an effort is being made to control the percentage of ownership in a Canadian institution. All right, we will accept that for the time being.

Mr. COMTOIS: That is the principle involved?

Mr. HART: That is right. But there is a second principle involved because they are limiting the operations of that bank by saying if at any time after the 31st of December they have outstanding total liabilities including paid up capital, rest account and undivided profits exceeding 20 times its authorized capital stock, and this I submit is discrimination because they are hampering...

Mr. COMTOIS: It is only if the control is more than 25 percent?

Mr. HART: That is right.

Mr. COMTOIS: Only if?

Mr. HART: That is right, but I think there are two sides to the question because they are limiting this bank which was and is a chartered bank of Canada, and this does not apply to any other chartered bank. There is no limitation on the total liabilities or deposits, which in effect is what they are, which the banks can accept from the public.

Mr. COMTOIS: But they would be limited if more than 25 per cent was owned by foreign capital. They would be limited under the same law.

Mr. HART: Oh, yes.

Mr. COMTOIS: So there is no discrimination.

Mr. HART: I submit there is because this has not arisen with any other chartered bank.

Mr. COMTOIS: But it could.

Mr. HART: This limitation on the total amount of deposits which they can accept from the public at large. There is nothing in the law restricting the total deposits.

*(Translation)*

Mr. COMTOIS: After the bill has been voted upon, there will be a limitation if the foreign control is above 25 per cent. It only applies in those cases where foreign control is over 25 per cent in any chartered bank.

*(English)*

Mr. HART: Yes, yes.

*(Translation)*

Mr. COMTOIS: Not only the Mercantile Bank, but any of the Canadian banks.

*(English)*

Mr. HART: Yes, but this would stop that because control beyond 25 per cent will not be permitted under another section of the proposed act. I would just say

again that at the present time there is no restriction on the amount of deposits which a chartered bank may accept.

(Translation)

Mr. COMTOIS: Mr. Hart, to come to the point, the Mercantile Bank, if it is excluded from the act, will be favoured?

(English)

Mr. HART: If they are excluded from the law they will be favoured.

Mr. COMTOIS: Yes.

Mr. HART: I cannot—

(Translation)

Mr. COMTOIS: As compared to any foreign bank.

(English)

Mr. HART: There is no other foreign bank involved in this particular case. You mean any other Canadian bank?

Mr. COMTOIS: Canadian or foreign, who wants to come here.

(Translation)

The CHAIRMAN: To put it more precisely, banks in the United States?

Mr. COMTOIS: If an English bank wanted to take over control of a Canadian chartered bank, then, there would be discrimination, because only the Mercantile Bank would have the right and not another foreign bank.

The CHAIRMAN: The City Bank which controls the Mercantile Bank?

Mr. COMTOIS: That is it.

(English)

Mr. HART: The law, if passed, would apply in future to any institution in which a foreign interest was attempting to obtain a measure of control or an interest in the equity of that particular bank. The point I am trying to make is that the Mercantile Bank is now a chartered bank of Canada operating within the framework of the present law, and therefore by introducing this proposed legislation it is going to hamper their operations but it does not apply to the other banks under the present law. I can see where in the future, if this limitation of 25 per cent ownership is put on, it will apply to everybody, of course, but up until the time that point has been reached or has been exceeded there are no restrictions on the chartered banks on the total amount of deposits which they may accept from the public.

The CHAIRMAN: I think what Mr. Comtois was driving at was the possible privileged position being given to the American bank which controls the Canadian bank in question, vis-a-vis their own competitors in the United States or in other countries of the world.

Mr. COMTOIS: That is it.

Mr. HART: Did the Dutch not have a privileged position when they established this bank?

The CHAIRMAN: I think Mr. Comtois' point is that at that time other interests in Holland or France or the United Kingdom or the United States could have come in and done the same.

Mr. COMTOIS: The same thing.

The CHAIRMAN: What Mr. Comtois may be driving at, and if I am not summarizing your thoughts correctly you may interrupt me, is if your suggestion that this law be passed is accepted, but this clause that seems to fall more heavily on the Mercantile Bank than the others be removed so that the Mercantile Bank will be able to expand to the same extent as any other Canadian chartered bank, then the American parent of that bank will have an entrée into the Canadian banking field which will not be available to any other foreign bank.

Mr. HART: That would be correct, Mr. Chairman, but the point I am trying to make—

The CHAIRMAN: Is that fair?

Mr. HART: Yes, but the point I am trying to make is as I mention in my brief, if I may read this one sentence again:

To take action to prevent recurrence of a situation to whatever extent such action may be desirable is one thing, but to take action against a single institution already operating within the law is quite another.

This is the point I make. I do not quarrel with taking action now which is going to apply in future to operations of financial institutions, banks, or whatever they may be, because this is going to apply to everybody who may wish in future to come in and establish in Canada. I do quarrel with the percentage, but this is not the point. I think it is an unnecessary restriction to put in this 25 per cent limitation, that is something else, but as a matter of principle if the law is passed and it applies to future operations of foreign corporations or entities coming into Canada, all well and good. Here we have a case, as I said, where this is an action against an institution already operating within the law, which is quite another case.

*(Translation)*

Mr. COMTOIS: Mr. Hart, if similar legislation were adopted in a state of the United States or in a foreign country, where you have a branch or a subsidiary that is your property, and the same legislation were adopted in the said state or country... would you obey that law?

*(English)*

Mr. HART: We certainly would have to abide by the laws of the host country, as I indicated in my brief. I think there would be a case, and that the Canadian government would have a strong case if they were disposed to do so, to voice very strong objection to that being done, but our case is weakened if we are going to do the same thing here that we do not want other people to do.

The CHAIRMAN: Mr. Hart, if a law in exactly these terms with respect to foreign banks were to be passed in the United States, which of your existing operations would be affected and to what extent?

Mr. HART: We would have to know what the law is. Presumably it—



The CHAIRMAN: This law here.

Mr. HART: No. I would not think it would affect their agency business because we are not operating down there under the federal reserve system. We are not operating like a United States bank. We are purely an agency, with the restriction of being unable to accept deposits from residents in New York state. We are not a part of the federal reserve system, as are other banks. So, this law which you suggest might not apply, I do not know, we would have to see the law. But our California operations—

The CHAIRMAN: I am referring to the clauses you are complaining about here.

Mr. HART: All right. If they put in a restriction such as this, or introduced legislation for this purpose, I think it might well apply to our operation in California. But we get into a point here because that is under California state law, it is not under federal jurisdiction. Now, there is a constitutional problem. I guess we have heard of this before even in Canada, whether or not federal law can superimpose itself on state law. I am not a lawyer and I cannot argue this point. It might not apply, but it might. I do not know. We would have to see what the law would be at the time. This act is a federal act. Banking is a federal matter in Canada, but in the United States—in California as an example—we operate under state law. We do in New York too, we operate under state law. It is a different type of operation, of course.

(Translation)

Mr. COMTOIS: Mr. Hart, could you tell me whether the proposed bill submitted in the United States by Senator Javits, was concerned with the revision of the Bank Act in Canada or was it directed generally to foreign banks operating in United States. There is nothing in this section referred to that supposes that it would apply directly to the Canadian situation?

(English)

Mr. HART: No, as the bill read at the time it applied to all foreign banks. They have not singled out Canadian banks. I think it is safe to assume that because of the proposed legislation here this is what gave rise to the so-called Javits bill.

The CHAIRMAN: Does Mr. Javits mention the Canadian legislation in any way?

Mr. HART: I am not aware of what he said in the Senate when he was speaking to the bill, Mr. Chairman. All I have before me is a copy of the proposed bill.

The CHAIRMAN: I can give you a copy of his text as well.

Mr. HART: Yes. I have not seen that, sir. Thank you very much. I take it there is nothing in here about Canadian banks as such. It is just all foreign banks, yes.

(Translation)

The CHAIRMAN: Other questions, Mr. Comtois? Mr. Chrétien would ask questions if you have no further questions.

Mr. CHRÉTIEN: Mr. Hart, you say that 75 2-g is discriminatory as now drafted, but are you not aware that the Act is not adopted yet and the Western Bank and the British Columbia Bank are about to have their charter accepted. Bank of Western Canada is a bank that is under way, it has obtained its charter and will be obliged to accept this provision of 75 2-g. If we remember the evidence of the chairman of a financial group that was to control the bank, Mr. Stevens, 75 2-g, according to him was to make it necessary for him to sell a greater number of shares than he had the intention of doing. So, 75 2-g is not discriminatory solely in regard to Mercantile Bank, but also discriminatory in regard to the Bank of Western Canada you agree?

(English)

Mr. HART: I do not recall that the Western Bank was going to have limitations on the amount of deposits they would be permitted to accept from the public, Mr. Chrétien.

Mr. CHRÉTIEN: Will they be obliged to follow that law? If Mr. Stevens himself has more than 25 per cent of the stock of the Western Bank he will be obliged to follow that law. So, Mr. Stevens will be obliged to sell a part of his interest in that bank because of that very section. So it is not discriminatory against—

Mr. HART: Mr. Chrétien, this is a bank which is not operating yet. You say they have received their charter, but there are other steps that have to be taken before they can open their doors for business.

Mr. CHRÉTIEN: If they wish they can start operations tomorrow morning. It is up to them.

Mr. HART: I do not know. I am not sure. They have not got a licence yet.

Mr. CHRÉTIEN: They are not ready yet but they obtained the charter before we passed that law and they will be obliged to follow that clause 75(2)(g) like every bank in Canada. So it is discriminatory to them too, if it is discrimination.

Mr. HART: I imagine they probably thought it was a pretty good move on their part to say they accepted this because, after all, they were eager to obtain a charter and they would not want to do anything that would perhaps upset the obtaining of that charter.

Mr. CHRÉTIEN: Yes, but they were not obliged to say so by any law at that time.

Mr. HART: No. That is quite true. They were not obliged to say so. I think it was probably a good move on their part to say so.

Mr. CHRÉTIEN: It was a warning by the committee of the same nature as the warning that the Mercantile Bank had from the Minister of Finance in 1963.

Mr. HART: I question that, Mr. Chrétien. This warning that was given to the Mercantile Bank, or to the First National City Bank of New York, was pretty vague at that time both as to the nature—

Mr. CHRÉTIEN: They would see that very soon, Mr. Hart.

Mr. HART: All right. —and the timing. It was subsequent to that that this proposed legislation was introduced.

Mr. CLERMONT: But you were not there, Mr. Hart, so how can you say it was vague?

Mr. HART: I do not know. I cannot speak with certainty because I was not there.

Mr. CHRÉTIEN: Just for your information, there is an article today written by Mr. Peter Newman which says that Mr. Rockefeller was supposed to have said at that time, "In other words, if we do so it will be at our own peril." So, do you think—

Mr. HART: You say "supposed to have said," but I was not there, Mr. Chrétien. I cannot argue this point.

Mr. CHRÉTIEN: If he said so, what do you think about that? It is reported in the press, and I know that is not the official record, but if he said so do you think it was a sufficient warning by the minister? If the last words by Mr. Rockefeller were—

Mr. HART: Well, Mr. Chrétien, I go back to a point I endeavoured to make earlier. Was it right and proper to give a warning of that kind? I do not know. I cannot argue from a point of law. But was it right and proper to single out one institution and give them a warning. The warning which subsequently—

Mr. CHRÉTIEN: I do not like it when you say to single out only one, because this clause 75 will apply to every bank in Canada. It will apply to the B.C. Bank, who have a charter right now, and they will be obliged to follow that clause.

Mr. HART: Well, certainly, it will apply to all the chartered banks in Canada.

Mr. CHRÉTIEN: And to your bank, too.

Mr. HART: That is right.

Mr. CHRÉTIEN: If tomorrow morning you want to buy 25 per cent of all the shares of your bank it is going to be difficult. If you want to do that your bank will suffer in its operations.

Mr. HART: If who wants to buy them, Mr. Chrétien? If anybody wants to buy them the bank will suffer? Why?

The CHAIRMAN: Any single individual.

Mr. CHRÉTIEN: They will be limited by clause 75(2)(g).

Mr. HART: This is very hypothetical, Mr. Chairman. I have not got the money to buy a 25 per cent share in my bank.

Mr. CHRÉTIEN: No, but if I want to do so.

Mr. HART: Quite apart from that, though—

Mr. CLERMONT: If Mr. Chrétien will allow me. Mr. Hart, you remarked was it wise of the then Minister of Finance to give such a warning. Was it wise of the American government to issue those guidelines to American businesses conducting business outside of the United States?

Mr. HART: I do not believe I said was it wise, Mr. Clermont. I do not think I questioned the wisdom of it. Perhaps I questioned the propriety of sounding a warning to one institution.



Mr. LEBOE: There was only one, though, was there not, to sound a warning to. I would think it was generous of the minister to sound a warning because they were the only ones who would be involved.

Mr. HART: Maybe it was.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Could I raise another point, Mr. Chairman?

The CHAIRMAN: Yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I would like to follow along the idea which Mr. Comtois had just now that the Mercantile Bank is, in effect, being given favoured consideration. If the government had not taken this action then, if you were going to avoid discrimination, it would have been necessary to demand that the owners of the Mercantile Bank of Canada divest themselves of 75 per cent of their foreign holdings. Had that not been done then it would have placed them in a favoured position vis-a-vis the other banks in Canada, would it not?

Mr. HART: I cannot quite see, Mr. Cameron—

Mr. CAMERON (*Nanaimo-Cowichan-The Island*): There is an advantage to having foreign ownership. They would be given a special privilege and they are today being given that privilege, which is being countered by another limitation on their operations.

Mr. HART: But, Mr. Cameron, the bank was 100 per cent foreign-owned when it was established in Canada.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes. But are you suggesting that we cannot change our ideas? I would like to remind you of this, Mr. Hart, that you only have temporary charters anyway. They are not in perpetuity.

Mr. HART: That is right.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It seems to me they should be subject to change when the government of Canada decides they should be changed.

An hon. MEMBER: Is that for one?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): If there is only one in that position, yes.

Mr. CHRÉTIEN: I have another question if I still have the floor, Mr. Chairman. A few years ago there was a brewery, Labatts Canadian brewery, or something like that, a Canadian company in that business, which decided to buy a company in the United States and they were not permitted to do so. Did the Bank of Montreal protest in the United States against that at that time?

Mr. HART: No, I do not think it was our place to protest.

Mr. CHRÉTIEN: Do you think it was discrimination against Canada?

Mr. HART: I am not in possession of the full facts of the case at the present time. I do not know whether we could say it was discrimination against Canada or discrimination against a company in the United States.

Mr. CHRÉTIEN: Yes, but you did not present any brief at that time?

Mr. HART: No sir. I am a banker, not a brewer.

Mr. CHRÉTIEN: You are here today just on principle, but the same principle was involved at that time. It is too bad you had not thought at that time to go there. That is all.

Mr. FULTON: Mr. Hart is a banker, he is not in external affairs.

The CHAIRMAN: Also, in fairness to Mr. Hart, I think he could quite legitimately say he has a greater direct interest in his own industry than in another one.

Mr. CHRÉTIEN: I know. It is just to liven up the discussion.

The CHAIRMAN: I suppose Mr. Chrétien could argue that both the products of the Canadian brewers and the products of the Bank of Montreal are basic commodities. They have that similarity.

Mr. HART: They are both highly liquid, anyway.

The CHAIRMAN: I will recognize Mr. Grégoire, in a moment. I wonder if Mr. Hart could clarify something for us. He mentioned that the agencies in New York are not part of the federal reserve system. He also mentioned that they can take deposits from people outside New York State, including other American residents. How are these agencies supervised? By what public body are they supervised?

Mr. HART: We receive our authority to operate from the Superintendent of Banks in New York. We receive an annual licence down there for which we must apply each year. The only restriction in the laws laid down by that banking authority is that we cannot accept deposits from residents of New York state.

The CHAIRMAN: Are there any reserve requirements under this?

Mr. HART: No sir. We are not members of the federal reserve system because we are an agency. If we had a branch down there we would come under federal reserve requirements.

The CHAIRMAN: In other words, you are not required by New York state law or any other law to maintain in your own accounts a certain percentage of your deposits?

Mr. HART: No.

The CHAIRMAN: Are you subject to the supervision in any way of Mr. Elderkin and his office with respect to the operation of your agencies?

Mr. HART: No, because the Bank Act deals only with banking in Canada. I do not think there is—

The CHAIRMAN: Mr. Elderkin, you seem to be making a negative motion.

Mr. ELDERKIN: I certainly would, Mr. Chairman. It is for the whole operation of the banks, no matter where it is conducted.

Mr. HART: Well that is true, I think I was off the beam there, Mr. Chairman, in that.

The CHAIRMAN: Do you make returns of information to Mr. Elderkin or the Department of Finance with respect to the agency?

Mr. HART: Oh yes, we meet all requirements for returns required by the minister through the Inspector General of Banks.

The CHAIRMAN: Have there been some new requirements in the past two years?

Mr. HART: Not that I recall, Mr. Chairman.

The CHAIRMAN: Tell me this, if the very worst happened, and I hope it will not and I personally doubt it, and you were not able to carry on any operations in the United States, would this destroy the solvency of the Bank of Montreal?

Mr. HART: Oh no, sir.

The CHAIRMAN: Would it move the Bank of Montreal from profit to a non-profit position?

Mr. HART: No, sir.

The CHAIRMAN: What would be your attitude if a foreign entity came to the Bank of Montreal and offered to buy 25 per cent of its shares?

Mr. HART: As I think I mentioned this morning, this is a situation which we think is hardly likely to arise because it would involve a pretty substantial sum of money. I think a foreign entity wishing to operate in this country might well prefer to set up a new operation under the law, whatever it might be at the time, but our shares are dealt with on the exchanges and a group of people associated together could buy up to 25 per cent or more under present legislation, but under the proposed legislation of course there are restrictions in the matter of association under section 52, and so on.

The CHAIRMAN: If this legislation were not passed, what would your reaction be to your bank falling under the control of a foreign entity?

Mr. HART: That is a rather difficult question to answer, Mr. Chairman.

The CHAIRMAN: Would you think it was a good or a bad thing from the point of view of the interests of Canada?

Mr. HART: It might be a good thing, in fact it could be a good thing if this would broaden the operations of the bank of the foreign entity which was purchasing a share of the equity in the bank. It could be a good thing.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): In what way would it broaden the operations, Mr. Hart?

Mr. HART: I think we would then have a foreign entity taking a greater interest in operations in Canada and it would perhaps help to broaden the operations. Again I get back to the international side, not the domestic side. I do not submit that any foreign entity which purchased shares in a Canadian bank would be in any better position to operate that bank in Canada than the bank itself would be at the present time, or any Canadian bank, but it might broaden the international operations of a bank which had a portion of its equity taken up by a foreign entity.

The CHAIRMAN: Let me see now, which is the largest bank in Canada?

Mr. HART: The Royal Bank of Canada.

The CHAIRMAN: You rank where?



Mr. HART: We are third in size by total assets.

The CHAIRMAN: What percentage of the total deposits of the chartered banks do you have?

Mr. HART: We are running around 20 to 21 per cent.

The CHAIRMAN: And you are suggesting there are circumstances under which it would be in Canada's interests if your institution was completely controlled abroad?

Mr. HART: I do not think the question was "completely controlled abroad", as I recall it, Mr. Chairman. A foreign bank taking an interest, for instance, in the Bank of Montreal, as you have suggested, might redound to the benefit of the country as a whole because of broadening the international operations of the bank.

The CHAIRMAN: I had in mind an interest sufficient to exercise effective control from a decision-making point of view.

Mr. HART: I really find it extremely difficult to answer that question because I think if a foreign bank wanted to purchase a substantial interest, or whatever that interest might be, in a Canadian bank, and you cited the example of the Bank of Montreal, presumably they would be doing so on the grounds of a good investment and would be satisfied with the way that bank was being operated.

The CHAIRMAN: As a Canadian would you look upon that with favour? I am speaking of control, not just investment.

Mr. HART: Yes. Again I find myself rather groping for words because I can only go back to my thesis that not just the Bank of Montreal but if Canada as a whole might benefit from having an institution which had broader international relationships and would help to expand trade, then I think it would be a benefit. I do not think that we could have any really strong objection.

The CHAIRMAN: You are saying that based on my example of control of decision-making? I want to be quite fair here.

Mr. HART: Yes, I know, but I think we would have to determine the purpose of a foreign entity coming in to take working control, or whatever share of the equity they might wish to acquire, of a banking institution. What would be the purpose behind it? I find it difficult from that standpoint, Mr. Chairman, to really deal properly with your suggestion.

The CHAIRMAN: If somebody had sufficient funds, would you say it would be a good investment to put them into the Bank of Montreal in order to have effective working control?

Mr. HART: I think they would have to determine themselves whether or not they thought it would be a good investment. I happen to have enough pride to think that the Bank of Montreal is a pretty good bank. We have been around a long time. But that does not necessarily sway the opinion of an investor. They would examine that matter very critically from their own standpoint.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Hart, you have spoken several times about the possibility of broadening the operations of the bank with particular reference to Canada's export trade. Can you tell me what

particular part your bank has played in the promotion and development of Canada's export trade? What particular role has it played?

Mr. HART: I think we have made a concerted effort, Mr. Cameron, to look after the requirements of companies in Canada engaged in the export trade so that we could assist them in financing their operations. I think this is perhaps the most important point of all. On the other hand, through our operations outside Canada, not just in the United States but in other countries as well, I think that we provide a good link between Canada and a country through our banking operations whereby we can perhaps assist in developing an interest in Canadian exports or Canadian products. We do try in that respect, too. But I think our main activity, of course, is financing Canadian exports to whatever country they may be going to around the world. This applies to all the Canadian banks. I think we have been a great factor, for example, in financing the sale of wheat to certain countries. I cite, perhaps, Poland as an example whereby we have provided long term financing, usually up to three years, which I think has been of great assistance to Canada. Of course, there are many other instances where we do financing for other commodities.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You have no branch in Poland?

Mr. HART: No sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Poland does not have a branch in Canada?

Mr. HART: No sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But this instance you cite, and I presume it is the first one that came in to your head, was carried out without any of what you consider to be desirable developments of a foreign bank being in Canada or you being in a foreign country?

Mr. HART: That is quite true, Mr. Cameron.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But does that not rather detract from your argument about the possibility of a foreign bank coming here and being able to broaden the operations of Canadian banks or the Canadian banking system?

Mr. HART: Who is to say, Mr. Cameron, until the matter is actually tested?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Let me ask you this. What particular role did your bank, or to the best of your knowledge any other Canadian bank—and when I speak of a role I am not speaking of the mere mechanical banking conveniences—play in the export trade from my province of British Columbia in pulp and paper, lumber products? Did it require some special service from the banks to develop that trade?

Mr. HART: I do not know to what extent I could say a special service. Naturally all the Canadian banks have participated in the financing of lumber and other products of the forest from British Columbia. It may very well be that we have contacts abroad where we have been able to be of assistance to Canadian firms seeking outlets for their products in these countries by introducing them to people that we know who might be interested in buying goods from Canada.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would this apply to our major exporters, such as the American oil companies that you spoke of earlier?

Mr. HART: I think they are pretty well established now in handling the sale of their own products, but I think—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): International Nickel, Canada Iron Ore, all our major exporters are really in a position to do it and all the services they require from the bank are the technical mechanical services, are they not?

Mr. HART: It may have been initially, Mr. Cameron, that they might have leaned rather heavily on the banking systems when they were starting up their operations, but now they have grown to a size and have established their own contacts around the world where perhaps we cannot perform the service we might have originally, but we can still assist in financing exports.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes. So, a foreign investment in your bank or any other Canadian bank, or the establishment of a foreign bank in Canada, would not materially affect our major export trade now, would it?

Mr. HART: No, but it might assist smaller companies who are now setting up operations, or who are operating in a small way of business, to expand their business in the foreign field. All companies usually start in a small way.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): These small ones started in a small way—well, it was not so very small, smallish—and presumably they relied on Canadian financial institutions.

Mr. HART: Yes, I would think so, largely to finance the extraction of the raw materials, the processing of the raw materials, the sales on credit of those processed materials, and so on.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It did not require a foreign bank to do that for them or a Canadian bank in a foreign country?

Mr. HART: It might very well have been the case that the importer of those materials into a foreign country would naturally have gone to his own bank over there to obtain financing so that he could pay cash or c.o.d. for the goods when they arrived. I am not in a position to argue that. This would be handled in a foreign country. But with competition these days, when you find that you have to sell on rather generous terms to foreign importers, then I think the Canadian banks do play an important part in financing that over whatever period of time is required. I just cite wheat as one example.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The point I was trying to bring out was just what substance there was to your argument that the operations of a bank might be broadened if a large part of its stock was in the hands of a foreign interest. I cannot see that it would broaden it in any way.

Mr. HART: Except that it brings us, perhaps, more closely in touch with the international field if you are extending your operations more worldwide than just operating within a smaller area. That is the point I was endeavouring to make.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Thank you.



The CHAIRMAN: I think Mr. Grégoire is the next name on my list. I am wondering whether or not the committee may feel—I am not trying to limit you, Mr. Grégoire—that we might be reaching the stage, following Mr. Grégoire's questions, where we have covered almost every area of the specific theme raised by Mr. Hart. I am not saying we have, I leave that to the consideration of the committee. I understand Mr. Hart will be available to us for an evening session, but we might consider using some of the time this evening to obtain Mr. Hart's views on some of the other matters we are considering as well. I am saying this subject to the proviso that Mr. Grégoire, who has other questions in this general area, would certainly be in a position to ask them. Certainly if other members have very pressing questions they feel they would like to ask on this subject they may do so as well.

*(Translation)*

Mr. CLERMONT: Mr. Chairman, to express my personal views, I think that after all the questions Mr. Grégoire wants to put, we will have received the information which Mr. Hart wanted to give us in regard to his brief. If we need further information in regard to the banking system, Mr. Hart could come or the representatives of the Bankers' Association could inform us.

The CHAIRMAN: I think Mr. Hart, as Chairman of one of the main banks, can express a valuable personal opinion in regard to some of the general questions that are now up for discussion. Maybe not. We will wait for Mr. Grégoire to put his questions, and then we will have a meeting to-night, will we not? That is a good idea.

*(English)*

Mr. CHRÉTIEN: Mr. Chairman, we can permit Mr. Grégoire to continue and ask his questions, and when he is finished I think it is the feeling of the committee that we should adjourn. We had a lot of explanations from the bankers' association and we do not want to take up too much of Mr. Hart's time anyway.

Mr. HART: Mr. Chairman, if I may say so, I would be very happy to attempt to answer any questions you may have, quite apart from the topic of this brief, if that is the desire of the committee. I am at your disposal.

*(Translation)*

Mr. GRÉGOIRE: Quite apart from the questions to put on Mr. Hart's brief I have another question to put to him. Just one other question.

The CHAIRMAN: If the Committee does not want to continue the session to-night, it is the right of the Committee to ask the Chairman not to have a meeting to-night. But to be fair to my colleague, Mr. Grégoire, as I have already said, we would recognize him for the purpose of putting questions with regard to the theme of Mr. Hart's brief I think we have the duty to allow him to put his questions, but as far as other fields that are not specifically mentioned in the brief are concerned, it is up to the Committee to decide whether they want it or not, or ask the Chairman to finish the sitting.

Mr. GRÉGOIRE: Anyway, we do not have a quorum, Mr. Chairman.

The CHAIRMAN: That is right.

Mr. GRÉGOIRE: According to article 288 it is the duty of the clerk to note that we do not have a quorum.

The CHAIRMAN: At the same time I would point out that I consider we are having an unofficial meeting for the purpose of taking evidence. If you do not wish to stay and ask your questions at this time, why, that is your privilege.

Mr. GRÉGOIRE: Do we reconvene at 8 o'clock, or what?

The CHAIRMAN: I am in the hands of the regular members of the committee.

Mr. COMTOIS: For my part I do not think there is any purpose in having a further meeting with Mr. Hart. I think we have grilled him just about as far as we can go.

*(English)*

Mr. HART: I would be very happy to come, gentlemen.

Mr. LEBOE: There will be other opportunities to get information from the Governor of the Bank of Canada on general banking.

The CHAIRMAN: It seems to be the consensus of the members here that we should remain and continue this unofficial evidence-taking session for the purpose of permitting Mr. Grégoire to ask his questions on the theme of Mr. Hart's brief, following which the session should be adjourned until next Tuesday when the next witness will be Mr. McLaughlin. Do I express the consensus of those present?

Some hon. MEMBERS: Agreed.

The CHAIRMAN: We are willing to stay at this time to permit you to ask the questions remaining that you feel you have to ask on Mr. Hart's brief.

*(Translation)*

Mr. GRÉGOIRE: Mr. Hart, in regard to your brief, I had only one point that I wanted to clarify in my own mind. When the Chairman of a big banking institution like the Bank of Montreal speaks to us of discrimination in regard to one of the existing banks, this is rather a serious matter. Mr. Hart, when I was listening to you give us your definition of discrimination, I was not entirely in agreement with you. I was not in agreement with your definition. Would you agree to the following definition, or at least the general definition of discrimination that it is a qualified act: In a more general sense, that it is an act that enables the drawing of distinctions either between different groups of the same type, or different types of the same genus. Would you agree to this definition of discrimination?

*(English)*

Mr. HART: I did not quite follow everything.

Mr. GRÉGOIRE: Do you accept as a definition of discrimination that it is a qualified act that would make a distinction or a separation between two different people of the same kind or two different groups of the same kind?

Mr. HART: I consider it discrimination when it applies to only one institution which is already operating within the framework of the bank under which it is chartered.

Mr. GRÉGOIRE: Would you accept the fact that it is a qualified act?

Mr. HART: A qualified act? You mean the act itself is qualified?

Mr. GRÉGOIRE: Yes.

Mr. HART: Yes.

Mr. GRÉGOIRE: Then would you accept that every qualified act can be qualified in its essence?

Mr. HART: An act which applies—

Mr. GRÉGOIRE: Every philosopher will admit that any qualified act can be qualified in its essence or because of accidents. Would you accept that definition? We are trying to define the kind of discrimination you are speaking about now.

Mr. HART: We are speaking of an act which applies to the chartered banks generally, and, yet there is embodied in the act proposed legislation which applies only to one of those chartered banks, and therefore it is qualified to that extent.

Mr. GRÉGOIRE: Does this discrimination you mention toward the Mercantile Bank of Canada come about because of accidents arising from the fact that a percentage of the Mercantile Bank of Canada belongs to foreign investments, or is it because in itself, in the essence of the article, it is discrimination, or is it only because of circumstantial facts related to the Mercantile Bank of Canada?

Mr. HART: If I follow you correctly, Mr. Grégoire, I think it would be circumstantial facts because the bank, as I stated before on more than one occasion, was wholly foreign-owned when it was established, and by virtue of the fact that the beneficial owner has changed from the hands of one foreign group to a group in another country, then it is apparently for this reason that this legislation has been introduced.

Mr. GRÉGOIRE: Then that clause would not necessarily be discriminatory against the Mercantile Bank of Canada in essence, but only because of circumstances related to the Mercantile Bank of Canada. It will not essentially be discrimination against that bank? Would you agree to that?

Mr. HART: I think it is discrimination because it applies to a bank which is already chartered. It would not be discrimination against an organization which wanted to come in and establish a new bank, because they would operate under the law or they would choose to come in or not.

Mr. GRÉGOIRE: That is not the question I am asking you, Mr. Hart. The clause here does not mention the name of the Mercantile Bank of Canada.

Mr. HART: That is right.

Mr. GRÉGOIRE: Notwithstanding the Mercantile Bank of Canada, do you consider that this clause 75 is essentially an article of discrimination against anybody?

Mr. HART: I would not say it is an article of discrimination if it were to apply now and in the future to the operations of chartered banks in Canada, but by virtue of the fact that it so happens that it bears heavily on one institution, which was already operating within the law, then from that standpoint I think discrimination has been exercised.

Mr. GRÉGOIRE: Then it is only accidentally there is discrimination because of the actual set-up of the Mercantile Bank of Canada?

Mr. HART: Accidentally perhaps, but suppose the ownership had remained in the hands of the original owners who established the bank—this is getting hypothetical again, Mr. Grégoire—would this legislation in fact have been introduced?



The CHAIRMAN: Mr. Hart, what is your basis for suggesting it would not have been introduced, inasmuch as the minister's statement to the House of Commons refers, in summarizing the intention of the government, to taking some steps to insure that the control of the Canadian banking system remains in Canadian hands. What basis or justification have you for saying that this proposed legislation is being proposed principally, or mainly, or only because of the nature of the transfer of foreign ownership?

Mr. HART: I can only submit, Mr. Chairman, that this might not have arisen had not the ownership changed.

The CHAIRMAN: What is your basis for saying that? Do you have any evidence to present?

Mr. HART: No, I have no evidence at all, Mr. Chairman.

The CHAIRMAN: It is your opinion.

Mr. HART: The bank was 100 per cent foreign-owned when it was chartered. If there was going to be legislation introduced, or if the government had any thought of introducing such legislation, presumably it would not have granted the charter in the first place.

The CHAIRMAN: Well, they are different governments.

Mr. HART: Are they?

The CHAIRMAN: Well, different administrations.

Mr. HART: Well, different administrations, yes.

The CHAIRMAN: Different parliaments.

Mr. GRÉGOIRE: Now, Mr. Hart, if the Mercantile Bank of Canada had not been owned 100 per cent but only 24 per cent by foreign investment, and by the same individual, in fact, then it would not have been discriminatory?

Mr. HART: You mean when the original ownership was set up?

Mr. GRÉGOIRE: Yes.

Mr. HART: No.

Mr. GRÉGOIRE: This article would not have been discriminatory if it had only been 24 per cent owned by the First National City Bank instead of 100 per cent?

Mr. HART: I still submit it would have been discriminatory to the extent that they were limiting the amount of liabilities which this bank could incur, that is, the amount of—

Mr. GRÉGOIRE: Only if it is more than 25 per cent of its issued shares, but I am speaking if they had had 24 per cent.

Mr. HART: Yes.

Mr. GRÉGOIRE: Then you would not find any discrimination in that?

Mr. HART: We are getting hypothetical again. If it was only 24 per cent would this have been introduced at all? I do not know, Mr. Grégoire.

Mr. GRÉGOIRE: Well, that is exactly the reason. We can see that this article then is not essentially a discrimination but only accidentally because it is 100 per cent owned by foreign investment. If it had been owned 24 per cent there would not have been any discrimination even if the article had been there.

Mr. HART: There would—

Mr. GRÉGOIRE: Even if the article had been there, if the First National City Bank had owned only 24 per cent of the shares there would have been no discrimination, is that a fact?

Mr. HART: If they had not introduced this limitation on the amount of deposits which the bank could accept. I go back again. I think there are two sides to this thing. One is the equity ownership and the other is restrictions on their operations as a chartered bank.

The CHAIRMAN: You are not suggesting to Mr. Grégoire that if one administration of the government has a policy today that successive administrations are bound in perpetuity to follow that policy?

Mr. HART: No, I am not suggesting that for one minute, Mr. Chairman. I am merely arguing again, to put it in somewhat more simple terms, that we are changing the rules for a bank in the middle of the game, which does not apply—

The CHAIRMAN: Where are these rules written down? What is the name of the game?

Mr. HART: The name of the game is chartered banking, Mr. Chairman.

The CHAIRMAN: Shall we change these rules every 10 years?

Mr. HART: Yes, you can change the rules or you can introduce new ones or you can update the regulations.

Mr. GRÉGOIRE: Mr. Hart, if the government of Canada increases in 1966 the interest rates which will not necessarily profit the small borrowers, is that changing the rule in the middle of the game for the small borrowers in Canada?

Mr. HART: We seem to be getting off onto another tangent now. Changing rates of interest I do not think is changing the rules of the game, Mr. Grégoire. After all, you operate in a very highly competitive atmosphere and we have, for instance, to pay going rates of interest to gather in deposit funds. If we do not do this somebody else will. It is competition that brings this about, and that certainly has a bearing on the rate of interest which you must charge. After all, it is a free market operation. I do not think you can classify it as changing the rules in the middle of the game. If you enter into a contract with a client to lend him a certain amount of money for a fixed period of time at a fixed rate of interest, then I think if you attempted to change that rate of interest before the loan matured you would be changing the rules in the middle of the game. But that, in fact, is not done. You enter into a contract.

Mr. GRÉGOIRE: Mr. Chairman, I have finished with that line of questioning. I have just one other question and I would like to ask it—

(Translation)

Mr. COMTOIS: A supplementary question, sir? A very short one.

The CHAIRMAN: Well, if Mr. Grégoire has finished.

(English)

Mr. GRÉGOIRE: I said I have one question, but if you have a supplementary question I will yield.

(Translation)

Mr. COMTOIS: Mr. Hart, do you admit that all the Canadian chartered banks are aware that every ten years, there is a revision of the Bank Act? So you

cannot claim that we are changing the rules in the middle of the game. Everyone is aware that every ten years the laws are revised or changed. And the argument does not stand up if you attempt to claim that the Mercantile Bank did not know that it was likely to suffer from changes in the law.

*(English)*

Mr. HART: All I can say, Mr. Comtois, in answer to that, as I have tried to explain before, is that the Mercantile Bank was and is a chartered bank of Canada operating under the same regulations as all the other chartered banks and which it continued to do from the date that it was formed.

The CHAIRMAN: For a ten-year period.

Mr. HART: For a ten-year period and sometimes a little longer.

An hon. MEMBER: Very good.

Mr. HART: But this legislation which is introduced now—and I am not arguing about the percentage ownership at this particular point—will restrict them in their operations as a chartered bank. It is true if another chartered bank finds that 25 per cent of its shares are owned by one resident or non-resident, the same rules are naturally going to apply. But until that happens there is discrimination against one chartered bank which has been operating under the law as it presently exists.

*(Translation)*

Mr. COMTOIS: Mr. Hart, the change asked is simply that this bank should sell 75 per cent of its shares on the Canadian market. That is all we are asking. We do not want to be discriminatory. We are only asking them to get rid of 75 per cent of their stock, and the operations of the bank are going to continue exactly as in the past.

*(English)*

Mr. CHRÉTIEN: Do you agree, Mr. Hart, that we have the same thing in the Western Bank?

Mr. HART: I beg your pardon, Mr. Chretien?

Mr. CHRÉTIEN: Do you agree with the proposition that we have exactly the same thing in the Western Bank and the Western Bank has a charter right now and article 75 does not apply, it is not yet allowed, but they will be obliged to go along with that.

Mr. HART: Well, they presumably agreed to that, Mr. Chrétien, when they sought the charter.

The CHAIRMAN: I think this question has been dealt with and we should proceed to get along.

*(Translation)*

Mr. GRÉGOIRE: Mr. Chairman, I have a question to put to Mr. Hart, as president of the Bank of Montreal, a chartered bank whose head office is in Montreal, in Quebec, and my question is this one: in the event of Quebec becoming an independent state, do you believe—

Mr. CHRÉTIEN: Hypothetical.



Mr. GRÉGOIRE: In the event of Quebec becoming an independent state, do you believe that the chartered banks should have a head office both in Quebec and in Canada, and in the event of this happening, how long would it take for the chartered banks to separate their operations and have a head office in Quebec and a head office in Canada?

*(English)*

The CHAIRMAN: I will interrupt at this point. I rule that this question is not relevant to the topic raised by the brief.

Mr. GRÉGOIRE: I said it was not a question on the topic of the brief. I said it was a general question. We are talking about foreign investments.

The CHAIRMAN: You said you had a question of general interest but I did not say I was going to accept it.

Mr. GRÉGOIRE: On what grounds do you refuse the question?

The CHAIRMAN: I declare the meeting adjourned.

## APPENDIX S

### Submission

to the House of Commons Committee  
on Finance, Trade and Economic Affairs  
regarding Bill C-222,  
An Act respecting Banks and Banking  
(by G. Arnold Hart)

I am particularly concerned about the provisions of section 75(2)(g) in the proposed Bill C-222, to which section I am strongly opposed, as a matter of principle, because of the discriminatory nature of the clause which is aimed directly at The Mercantile Bank of Canada. The clause reads as follows:—

“(2) Except as authorized by or under this Act, the bank shall not, directly or indirectly,

(g) at any time after the 31st day of December, 1967, have outstanding total liabilities (including paid-up capital, rest account and undivided profits) exceeding twenty times its authorized capital stock if more than twenty-five per cent of its issued shares are held by any one resident or non-resident shareholder and his associates as described in section 56.”

In specific terms, I have the following observations to make with respect to this section:—

- (a) The Mercantile Bank of Canada was granted a charter by the Government then in power in the full knowledge that the new bank was under foreign ownership. The Bank of Montreal did not oppose the granting of a charter to this newly formed institution. In adopting this attitude we took the view that open competition in banking was desirable in the interests of the Canadian economy and that there should be no objection to the entry of a foreign-owned bank, providing, of course, that its operations were subject to the same measure of regulation and control that applied to already established banks in Canada. We were also cognizant of the fact that it would be inconsistent to oppose the entry of a foreign-owned bank into Canada in the light of the then existing and prospective extension of the operations of Canadian banks in other countries.
- (b) Even though foreign-sponsored and foreign-owned, no special restrictions whatsoever were placed on The Mercantile Bank of Canada to hamper its operations and it was recognized as a chartered bank with power to operate in the same way as other chartered banks in Canada under the provisions of the existing Bank Act.
- (c) At the time the ownership of the Mercantile Bank changed hands, there was no legal obstacle to such step and the new owners acted quite within their rights under existing law. Because the nationality

of the ownership changed from Dutch to U.S., the rankest kind of discrimination was threatened and subsequently introduced in a proposed revision of the present Bank Act and continued in the revised Bill now before Parliament, with an added provision of a deadline of 31st December, 1967.

- (d) Not only is the proposed legislation affecting the Mercantile Bank discriminatory, but also, in my opinion, it is definitely a backward step in a free and democratic society. To take action to prevent recurrence of a situation to whatever extent such action may be desirable is one thing, but to take action against a single institution already operating within the law is quite another.
- (e) I submit that the reputation of Canada is at stake if, in the international field, we attempt to act in such an arbitrary and discriminatory manner—an action which can only lay us open to retaliation at the hands of others.
- (f) I hold no brief for the Mercantile Bank or its parent institution, but there is a matter of principle involved here and it is on this basis I am so strongly opposed.
- (g) The Bank of Montreal has operated in the international field longer than any other Canadian bank and in so doing has invariably behaved as a good corporate citizen in whatever host country is involved. More important, we believe that the extension of our facilities into other countries has played a constructive part in facilitating the development of Canada's international, commercial and financial contacts.

For example —

(1) We operate the oldest foreign bank agency in New York City, having established there in 1859, and these operations have continued uninterrupted, under annual licence granted by the New York State Banking Authority, for 107 years.

(2) The Bank of Montreal (California), a wholly-owned subsidiary of the Bank of Montreal that stems from our San Francisco office, which commenced operations in 1864, is one of the oldest banks operating under the laws of the State of California.

(3) The Bank of Montreal was the first Canadian bank to establish a branch in the United Kingdom and has carried on a banking business in London since 1870.















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*The Clerk of the House.*



HOUSE OF COMMONS

First Session—Twenty-seventh Parliament

1966

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STANDING COMMITTEE

ON

FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. HERB GRAY

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MINUTES OF PROCEEDINGS AND EVIDENCE

No. 29

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TUESDAY, DECEMBER 6, 1966

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Respecting

Bill C-190, An Act to amend the Bank of Canada Act.

Bill C-222, An Act respecting Banks and Banking.

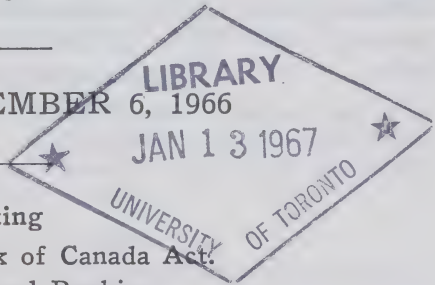
Bill C-223, An Act respecting Savings Banks in the Province of Quebec.

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WITNESSES:

W. Earle McLaughlin, Chairman and President, *The Royal Bank of Canada*; J. W. Powell, President, *RoyNat Limited*; Louis Hébert, President, *La Banque Canadienne Nationale*; C. F. Elderkin, Inspector General of Banks.

ROGER DUHAMEL, F.R.S.C.  
QUEEN'S PRINTER AND CONTROLLER OF STATIONERY  
OTTAWA, 1966



STANDING COMMITTEE  
ON  
FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. Herb Gray

*Vice-Chairman:* Mr. Ovide Laflamme  
and Messrs.

Addison,	Comtois,	Leboe,
Basford,	Flemming,	Lind,
Cameron ( <i>Nanaimo- Cowichan-The Islands</i> ),	Fulton,	McLean ( <i>Charlotte</i> ),
Cashin,	Gilbert,	Monteith,
Chrétien,	Irvine,	More ( <i>Regina City</i> ),
Clermont,	Lambert,	Munro,
Coates,	Lamontagne,	Valade,
	Langlois ( <i>Mégantic</i> ),	Wahn—(25).
	Latulippe,	

Dorothy F. Ballantine,  
*Clerk of the Committee.*

## MINUTES OF PROCEEDINGS

TUESDAY, December 6, 1966.

(57)

The Standing Committee on Finance, Trade and Economic Affairs met at 11.10 a.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Cameron (Nanaimo-Cowichan-The Islands), Chrétien, Clermont, Flemming, Gilbert, Gray, Laflamme, Lambert, Leboe, Latulippe, McLean (Charlotte), Monteith, More (Regina City)—(13).

*Also present:* Messrs. Grégoire and Southam.

*In attendance:* Messrs. W. Earle McLaughlin, Chairman and President, The Royal Bank of Canada; J. W. Powell, President, RoyNat Limited; Louis Hébert, President, Banque Canadienne Nationale; C. F. Elderkin, Inspector General of Banks; Miss M. R. Prentis, research assistant.

The Chairman read into the record a letter from Mr. Alastair Macdonald, Parliamentary Agent for The Mercantile Bank of Canada whose representatives were scheduled to appear before the Committee on Thursday, December 8th. Mr. Macdonald's letter explained that Mr. Robert MacFadden, President of the Mercantile Bank was ill and requested a postponement of the hearing.

On motion of Mr. Flemming, seconded by Mr. Chrétien,

*Resolved*,—That the Committee accept Mr. MacFadden's request for a deferment of his hearing; that the Chairman be directed to arrange another date for his appearance and that the question of a witness for Thursday's meeting be referred to the Sub-Committee on Agenda and Procedure.

On motion of Mr. Leboe, seconded by Mr. Flemming,

*Resolved*,—That the two papers prepared by the research assistants referred to at the meeting of December 1st, be printed as appendices to this day's Minutes of Proceedings and Evidence. (*See Appendix T—Bank Service Charges and Appendix U—Instruments Eligible for Re-discount at Federal Reserve Banks.*)

The Committee resumed consideration of the banking legislation and the Chairman introduced the witness, Mr. McLaughlin, who summarized his brief, copies of which had previously been distributed to the members. In accordance with the resolution passed at the meeting of October 13, 1966, the brief is attached for printing. (*See Appendix V.*)

Mr. McLaughlin was questioned, and Messrs. Powell and Hébert were called and questioned. Mr. Elderkin was also questioned.

The questioning continuing, at 12.45 p.m., the Committee adjourned until 3.45 p.m. this day.



AFTERNOON SITTING  
(58)

The Committee resumed at 3.55 p.m. this day, the Vice-Chairman, Mr. Laflamme, in the Chair.

*Members present:* Messrs. Cameron (*Nanaimo-Cowichan-The Islands*), Clermont, Flemming, Gilbert, Gray, Laflamme, Lambert, Leboe, Latulippe, Lind, Monteith, More (*Regina City*), Wahn—(13).

*Also present:* Mr. Grégoire.

*In attendance:* Mr. McLaughlin, Mr. Elderkin, Miss Prentis, and Mr. Denis Baribeau, research assistant.

Questioning of Mr. McLaughlin was continued.

At 5.30 p.m. the Chairman resumed the Chair.

The questioning having been concluded, the Chairman thanked the witness for his useful answers to a wide variety of questions.

At 6.15 p.m. the Committee adjourned until 11.00 a.m. Thursday, December 8, 1966.

Dorothy F. Ballantine,  
*Clerk of the Committee.*

## EVIDENCE

*(Recorded by Electronic Apparatus)*

TUESDAY, December 6, 1966.

The CHAIRMAN: Gentlemen, I call the meeting to order. Before beginning there are one of two procedural matters to be dealt with. First of all, I think I have had distributed to the members a copy of a letter I received late yesterday from the solicitor for the Mercantile Bank of Canada and while further copies are being distributed I will read the letter. It is addressed to myself as Chairman of this Committee. It reads as follows:

Dear Mr. Gray:

I am acting as Parliamentary Agent for The Mercantile Bank of Canada and a Hearing for the Bank has been scheduled for Thursday next.

Unfortunately, Mr. Robert MacFadden, President of the Bank, who will head the delegation has had an attack of pleurisy and, although he has recovered to some degree, will be unable to appear before the Committee for the Hearing.

Needless to say, although the inconvenience to the Members of the Committee is greatly regretted, I am forced to ask you, on behalf of the Bank, to grant an adjournment of the Hearing until early in the New Year.

Yours truly,

Alastair Macdonald.

It is signed by Alastair Macdonald of the Ottawa law firm who has been representing the bank in its contacts with the Committee. The reason I am bringing this up at this time is that there obviously has not been time to have a meeting of the steering committee so they could report to you, and since this Committee had already agreed to hear the Mercantile Bank next Thursday I thought as our first item of business I would bring this to your attention and ask for your suggestions in this regard in the light of the request made quite definitely by the Mercantile Bank through their solicitor.

Are there any comments?

Mr. MONTEITH: Mr. Chairman, you have not been in touch with the solicitor and I am wondering if for argument's sake a week from tomorrow might be feasible.

The CHAIRMAN: With respect to this letter, I have had some contact with him which was in effect to confirm what was in the letter. I really did not definitely discuss another date but I suppose that could be done.

Mr. LAMBERT: Mr. Chairman, I do not want to scare Mr. McLaughlin at all but it is conceivable I think—not only on account of the brief but other matters—the examination of Mr. McLaughlin might take more than today. The

one point I would like to make though is to suggest to you, sir, right before the members of the Committee, that is high time we had the Minister of Finance here before this Committee because with many of the witnesses on particular matters of the bill we are punching at pillows. The changes are being proposed by the government and there is absolutely no indication of the government's thinking. You cannot examine the witnesses, shall we say, in reply to the government's proposal to make changes. That is going to, perhaps in some cases, result in our having to have or consider to bring some of the witnesses back. I think that is highly unfair.

I think the steering committee could take up the question of having the Minister appear before the Committee for the next fortnight or so to justify some of the changes that are proposed in this act.

Mr. CHRÉTIEN: I think the Minister is willing to come as soon as the Committee wants to see him.

Mr. LAMBERT: I am not suggesting that the Minister is not willing to come. I hope that was not the impression I gave. I hope Mr. Chrétien's skin is not that thin. It is merely the matter of the sequence.

The CHAIRMAN: I should say in fairness to all concerned it had been, as I understood it, the general consensus of the steering committee, although there had not been a resolution to this effect, that the Minister of Finance be a witness before the Committee after we heard the people from outside of what you might call the government sector. If we wish to change our direction in that regard we can do so. We can discuss this at our steering committee meeting which is scheduled for tomorrow noon. If anybody is unable to be present we can have other consultation before or after.

With respect to the specific matter of the adjournment requested by the Mercantile Bank, would the Committee in effect accept this request and be willing to give the steering committee, together with the Chairman, the authority—which in fact they would have anyway—to fix a new date. Is that agreeable.

Mr. FLEMMING: I so move.

Mr. CHRÉTIEN: I second the motion.

The CHAIRMAN: It is moved by Mr. Flemming and seconded by Mr. Chrétien that my suggestion will be the wish of the Committee. We are agreed in that regard.

Motion agreed to.

The CHAIRMAN: Second,—

Mr. LEBOE: Mr. Chairman, just on that point, perhaps we could give consideration to the request made by Mr. Lambert in connection with the minister if this space is going to be open.

The CHAIRMAN: I have made a note of that and we will look into it tomorrow.

The next point is another small procedural point. Mr. Clermont has been kind enough to give us consent to have two memos prepared at his request. I referred to them at the last meeting and distributed them to the Committee. Is it the wish of the Committee that these two documents be appended to our proceedings? I will ask for a motion in that regard.



Mr. LEBOE: I so move.

Mr. FLEMMING: I second the motion.

Motion agreed to.

Mr. CLERMONT: Mr. Chairman, I hope that I will get my original copies back because I have not received them yet. The copies were distributed to the members but I hope I will get my copies back.

The CHAIRMAN: Well, the Clerk informs me that they were sent back. Perhaps you will have to check on the machinery of the house in this regard. Perhaps a messenger is finding the copies of great interest and is reading them before handing them back to you.

Mr. CLERMONT: All right. Thank you.

Mr. MONTEITH: Mr. Chairman, one other matter of procedure, if I might raise the question; I wonder if Mr. Chrétien has any idea of when the deposit insurance legislation is going to be before us.

Mr. CLERMONT: Mr. Chrétien just left. He has to take a train at 12 o'clock.

The CHAIRMAN: Yes. I think he has to give a speech this afternoon. He may be dealing with some weighty matters.

Mr. MONTEITH: Maybe the Chairman has an indication.

The CHAIRMAN: At this point I can give you no further information beyond what—

Mr. MONTEITH: I had better ask the Minister on Orders of the Day.

The CHAIRMAN: That is an idea which might be helpful. At the moment I have no information beyond the information that you and I both obtained on the extension bill which was being discussed in the house.

Our witness this morning is Mr. W. Earle McLaughlin, Chairman and President of the Royal Bank of Canada. His brief has been distributed to the members and I would invite Mr. McLaughlin to present his brief. Ordinarily we ask the witnesses merely to summarize their brief and I note you have a summary, Mr. McLaughlin. I would invite you to proceed at this time.

Mr. W. EARLE McLAUGHLIN (*Chairman and President of the Royal Bank of Canada*): Thank you very much. Mr. Chairman and gentlemen, my brief is quite a short one but I do have an even shorter summary. The brief deals with one topic only, namely, the case for exempting RoyNat Ltd. from the provisions of Clause 76 of Bill No. C-222, which would require each of the stock holding banks—The Royal Bank of Canada and Banque Canadienne Nationale—to reduce its voting stock interest in RoyNat to 10 per cent by July 1, 1971. The case for exemption is supported by the following four points:

(1) The proposed provision is retroactive. RoyNat was established when no such provisions existed. The present owners of RoyNat established it to fill a gap in the financial system.

(2) the proposed provision is not only retroactive, it amounts to penalizing present and future initiative. That is not the way to encourage useful innovations and improvements in the financial system. The Porter report indicated that it was undesirable to have, and I quote from page 371 of said report:

—legislation inhibit useful innovations and improvements in the financial system by preventing or unduly restricting the participation of banking institutions in new joint ventures with other businesses or with other members of the financial community.

(3) The Export Finance Corporation of Canada Ltd. specifically exempted in clause 76(7) is owned by all the chartered banks with no bank in a position of control. RoyNat is owned by two banks and three trust companies with no bank or trust company shareholder in a position of control. Hence, I submit that RoyNat should be treated in the same way as The Export Finance Corporation of Canada Ltd.

(4) The Porter Report specifically pointed out the advantages offered by RoyNat, so that it would appear that the Porter Commission would exempt RoyNat from the proposed provisions.

Much of RoyNat's success is due to its close association with its two chartered bank shareholders, an association that could be lost if the proposed provision came into effect. This association enables RoyNat to raise its money from the public at less than it would otherwise have to pay which helps to keep its charges down. This association also allows RoyNat to offer a wider range of services than otherwise. Furthermore, association with the two banks provides it with over 1,700 branch offices from which originate 57 per cent of all inquiries received by RoyNat.

If the two banks had to reduce their interest in RoyNat to 10 per cent it might not pay the shareholding banks to provide these facilities to RoyNat.

Finally, RoyNat's continued growth will require increased capital, and it is far easier to raise this needed capital from five shareholders than say from 5,000. Thus, enactment of clause 76 of Bill No. C-222, without providing for the exemption of RoyNat, would reduce the effectiveness of RoyNat. This is important because the chartered banks operating on their own could not duplicate the RoyNat type of operation. The banks cannot enter into longer term lending to any great extent because of the short-term nature of their borrowed funds. Moreover, it is doubtful if the banks would be interested in moving into the medium size business field now serviced by RoyNat.

A further disadvantage to a forced reduction in RoyNat ownership by the two chartered banks could be to transfer ownership and control of this Canadian institution into the hands of foreign interests.

Therefore, both for reasons of principle and for highly practical reasons as well, and in the national interest, the submission concludes that Bill No. C-222 should be amended so as to have the name "RoyNat Ltd." after the name "Export Finance Corporation of Canada Ltd." in clause 76(7).

As I pointed out in my formal brief, I am pleased to say that Mr. Louis Hébert, President of the Banque Canadienne Nationale, who is here today, supports this presentation.

The CHAIRMAN: Thank you, Mr. McLaughlin. Our usual procedure has been to invite the members of the Committee to ask questions on the issue or issues raised specifically by the brief. When we have exhausted this line of questioning we would then allow the members of the Committee to ask questions on other matters relevant to the legislation referred to us for study. I would now like to recognize Mr. Clermont, followed by Mr. Lambert. I would ask the other members to signify in the usual manner. Mr. Cameron, Mr. McLean and Mr. Monteith.

(Translation)

Mr. CLERMONT: Mr. McLaughlin, the RoyNat Corporation has on the 30th of April, 1966 1,300 loans or \$149,000 on the average. What is the amount of loans issued by RoyNat? What is the criteria that was used in deciding on the loans to be made? What is the maximum that RoyNat wants to loan or can loan? Does it depend on the credit of the company, or do you have other criteria, let us say that your Corporation does not make loans beyond \$200,000 or 250,000?

(English)

Mr. McLAUGHLIN: Mr. Clermont, I can answer that partially. I must make clear that I have nothing to do whatsoever with the day-to-day operations of RoyNat.

(Translation)

Mr. CLERMONT: You were to be accompanied by Mr. Powell who is the president or—

(English)

Mr. McLAUGHLIN: Mr. Powell is in the audience if you wish to ask any technical question on operation of RoyNat. He is available to come forth.

The CHAIRMAN: Mr. McLaughlin, I think the members of the Committee will agree with me when I suggested it would be helpful if he was with you. Perhaps they would wish to refer the more technical questions to Mr. Powell and I would ask Mr. Powell to step forward. Is Mr. Hébert with us as well?

(Translation)

Is Mr. Hébert here? Can he please come forward. Could we have the privilege of hearing Mr. Hébert. Would they please be seated next to Mr. McLaughlin and Mr. Powell so we can have a good bilingual team?

(English)

Mr. Powell, I see that you are in the middle here. It probably reflects the corporate structure of RoyNat.

Mr. J. W. POWELL (*President, RoyNat Ltd.*): That is quite true.

The CHAIRMAN: You are between Mr. McLaughlin and Mr. Hébert. I think this may aid in the consideration of the matter you wish to bring before us.

Mr. McLAUGHLIN: I am quite happy to answer questions on the principle of RoyNat but not on the detail. I am not a director and I have no knowledge of its day-to-day operations.

(Translation)

Mr. CLERMONT: Mr. McLaughlin, the brief you submitted and the annual report of the Corporation gives a good deal of information. I would be interested in knowing something about the internal activities of your Corporation if I could?

(English)

Mr. McLAUGHLIN: Mr. Clermont, on the question of the internal activities of the corporation I will refer you to Mr. Powell who is the president and the chief executive officer.



The CHAIRMAN: Mr. Powell, are you prepared to deal with Mr. Clermont's question?

Mr. POWELL: I am awfully sorry but my ear piece was not working when you started off, sir. The first question, I understand, was dealing with the—

*(Translation)*

Mr. CLERMONT: Do you want me to repeat the question, Mr. Powell. Are you getting it now? This is my question; since this Corporation came into effect you have made loans to 593 persons, groups or companies at an average of \$149,000 per loan. In your rules, do you have a ceiling on the loans that you make to companies, or is the criteria on the solvency of the customer. What is the criterion used in deciding the ceiling of the loan extended?

*(English)*

Mr. POWELL: Well, number one, the smallest loan we make is \$25,000 and we go up to as high as \$1 million or more. We have 10 loans of more than \$1 million on our books. The criteria is based completely on each individual transaction. If someone comes to us for some financing we first of all look at the type of industry, the financial position of the business that is applying for the loan, the management—which is very important—and also the continuity of management, so we will have good management in the business through to the end of the payments on our loan.

We also look to the cash flow of the business which is important to service the debt. We have to, of course, also look for security and our security has consisted mainly of first mortgage bonds on real estate, machinery and equipment—floating charge. Does that answer your question, sir?

*(Translation)*

Mr. CLERMONT: You mentioned that in your books you have ten loans of more than one million. Without divulging the names of persons, could you tell us what is the highest loan you have granted to date? What is the highest loan issued?

*(English)*

Mr. POWELL: The highest loan we granted to date is one to a group of companies in the same family, so to speak, of \$2 million.

Mr. McLAUGHLIN: Mr. Clermont, may I supplement that answer by saying that one of the principles behind the formation of RoyNat was to enable it to provide long-term financing to those companies which, because of the term, would find it difficult to get it from a chartered bank and because of the size would find it difficult to get it in the public market. That is the reason why there are very few over \$1 million. Basically, over \$1 million—if you have a sound proposition—you can go to an investment dealer and have a public issue. Under \$1 million it is more difficult and more expensive. That is the gap that RoyNat is trying to fill.

*(Translation)*

Mr. CLERMONT: I think, Mr. Powell, that your Corporation has loaned 75 million of which 60 million in 1966, is that right?

(English)

Mr. POWELL: Sir, that is not quite the right figure. Our total loans; that is, investments we have made in the company since inception to October 31, last, was \$108,046,000.

(Translation)

Mr. CLERMONT: In 1965 your annual report of the 30th of April, 1966 mentioned short-term loans of \$10,200,000.

Was this loan by the banks that are the shareholders, was it in shares purchased by the public?

(English)

Mr. POWELL: Oh, I see what you mean. I am sorry, I was looking for an exact figure. That represents our short-term borrowing from the public.

Mr. CLERMONT: From the public?

Mr. POWELL: That is correct.

(Translation)

Mr. CLERMONT: What was the interest rate on these short term loans?

(English)

The rate of interest, not the total—

Mr. POWELL: Unfortunately, I cannot give you that figure because the rates vary. In other words, they varied with market conditions throughout the time we were borrowing. We borrow basically at the same rate as the finance business would borrow on the short-term money market at any given moment and those rates vary from day to day. They have increased rather substantially during the last two years.

(Translation)

Mr. CLERMONT: In the annual report you mention the fact that these loans have helped the setting up of 64 new corporations and enabled the purchase of 37 other companies. I would like to know whether these 37 companies were Canadian-owned or foreign-owned?

(English)

Mr. POWELL: I would say this: That every one of our clients—I should not say every one—but a very, very small percentage is foreign owned. In other words, they might be a subsidiary of a foreign corporation. This is just a guess, mind you, but I do not think there are more than five or six on our books that are of that type. The rest are all Canadian corporations.

(Translation)

Mr. CLERMONT: If the Royal Bank of Canada and the National Canadian Bank were to sell the surplus over 10 per cent of shares they hold in that corporation, what would be the sum involved in the case of each bank?

(English)

Mr. McLAUGHLIN: The Royal Bank of Canada—

(Translation)

Mr. CLERMONT: Mr. McLaughlin, I believe the percentage would be 75 per cent for the Royal Bank and 70 per cent for the National Canadian Bank, but I would like to know the amount in dollars.

(English)

Mr. McLAUGHLIN: The capital stock is \$10 million so that if it is 70 per cent it is \$7 million.

(Translation)

Mr. CLERMONT: For both then?

(English)

Mr. McLAUGHLIN: I am sorry, 70 per cent of our share. The Royal Bank of Canada holds 41.5 per cent which is \$4,150,000. The Banque Canadienne Nationale holds 34 per cent. The total of the two is 75.5 per cent, or \$7,550,000. We would have to be down in total to \$2 million, which means \$5,550,000. Five and one half million dollars, in round figures, would have to be disposed of in some way in some place.

(Translation)

Mr. CLERMONT: In your yearly report of April 31, 1966, under distribution of investments, sub-heading: Food and Drinks, the figure reads 9.8 per cent or \$7,402,000. Do you know what the amount will be for food and drink for next year?

(English)

No, not next year. That is not true. I did not say that.

Mr. POWELL: Sir, do you mean are all our investments that we have made as diversified now as they were at April 30.

Mr. CLERMONT: Mr. Powell, I was not finished. I said, according to your annual report, dated April 30, 1966, you had advanced for food and beverages over \$7 million. My question is: Have you any idea of the figures advanced, not for food but for the other kind of—

Mr. POWELL: The breakdown between food and beverages? No, we do not have that; I am sorry.

Mr. CLERMONT: You do not have it for the wholesale and retail trade either?

Mr. POWELL: We do not maintain a breakdown of that. If I do not have it in the statement, we do maintain it religiously because we like to keep our investments diversified in all areas of business.

(Translation)

Mr. CLERMONT: I would like to know if the intention of the Royal Bank is to sell bonds in the near future?

(English)

Mr. McLAUGHLIN: Is it the intention of the Royal Bank of Canada to sell bonds?

Mr. CLERMONT: Oh, no.

Mr. McLAUGHLIN: Oh, RoyNat.



Mr. POWELL: We will have to sell more secured notes in due course as soon as the funds are required. It would appear that possibly another issue is not foreseen until next year.

Mr. CLERMONT: Thank you, Mr. Chairman.

The CHAIRMAN: I now recognize Mr. Lambert.

Mr. LAMBERT: Mr. McLaughlin, prior to the introduction of the previous bill to amend the Bank Act and this particular bill, had you received any intimation that the government had any objection to the operations of RoyNat?

Mr. McLAUGHLIN: None whatever.

Mr. LAMBERT: Or that this type of operation was not bona fide—I should not say bona fide. It was not, shall we say, in the good graces of government thinking.

Mr. McLAUGHLIN: None whatever. I had the feeling it was welcome.

Mr. LAMBERT: There had been no informal discussions or representations made to the participants in RoyNat or—perhaps this is hearsay—in the operations of Kinross, which is a similar type of operation, that these were not strictly within the limits of government thinking. It is unfortunate that we do not have the government's ideas in this regard as to why this particular step has been contemplated. That is the only question I had.

The CHAIRMAN: I now recognize Mr. Cameron followed by Mr. Monteith and Dr. McLean.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. McLaughlin, in view of the provision that is in the new bank bill which is now before us and which will permit banks to issue debentures, do you think there is any possibility of banks engaging in the type of work that RoyNat has been engaged in in the past?

Mr. McLAUGHLIN: Mr. Cameron, I would suggest that that is probably unlikely because there is another clause of Bill No. C-222 which permits the banks to go into residential mortgages and that takes long-term money. There is a limit both on the amount of mortgages and the amount of debentures but the limit on the debentures is more restrictive than on mortgages. I would think that when the bill is passed, if it goes through this way, probably a bank would mentally allocate the proceeds of such debentures as it can issue to its mortgage business. That does not leave anything left over for the term lending to small businesses. So, I personally do not look to the funds which would be raised from debentures to be of any use in the type of business that RoyNat is doing in a bank.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You mentioned in your brief that 57 per cent of the inquiries about RoyNat come from the branches of the two banks involved. I was wondering if you could tell us something of the role that is played by the three trust companies who are shareholders in RoyNat.

Mr. McLAUGHLIN: The three trust companies play a double role, if you like. They play the same role as the branches of the two chartered banks in having pamphlets and literature and making the fact that RoyNat exists known to their clients. They have a second role in that in many instances the security given to RoyNat is in the form of a mortgage bond issue and the three trust companies act as trustees at special low rates. It is an advantage to the borrower because it is a little cheaper than the normal course to have a bond issue. It is a dual role.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Powell, you mentioned that you thought that about five or six of your clients would be foreign owned corporations. Could you give us any idea of what proportion of your total loans they would represent.

Mr. POWELL: Mr. Cameron, as I mentioned before, that is a guess, my figure of five or six. To take a rough guess now I would say that there is not more than \$300,000 or \$400,000 involved that I can think of at the moment, generally small businesses which are subsidiaries of larger firms.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The reason I asked this is that I noticed that in one of the areas of financing that you have listed in the report there is petroleum. I was wondering if these are Canadian petroleum operations that you finance.

Mr. POWELL: Yes, they are all Canadian petroleum. I can say that mainly they are in the drilling business, and so forth.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then you have another item under "personal services" which includes hospitals. I was wondering if this includes loans to public or semi-public bodies to operate hospitals.

Mr. POWELL: They are private hospitals as such. Let us say, homes for the elderly and those who require treatment where they can live in more or less all the time.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You do not engage in any wider hospital finance?

Mr. POWELL: No, we do not do that at all.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): To return to the question I was asking you just now, Mr. McLaughlin; If the restrictions on the issuance of debentures were relaxed do you think there would be any advantage to the banks, shall I say, departmentalizing their operations rather than establishing separate entities such as RoyNat?

Mr. McLAUGHLIN: That is a very difficult question to give an answer "Yes" or "No" to, Mr. Cameron. RoyNat, I think, has a distinct advantage. It has branches in each province with specialized services. The chartered banks so far have tried to maintain in each of their many branches the same facilities for customers. It does not matter whether you are a customer at Frobisher Bay or in Ottawa you can get the same services. For specialized services like this it is much better to concentrate it in a few places and that is why I think a specialized institution like RoyNat can do a better job, more concentrated, than to have it spread out so thin that a specialized officer is perhaps doing nothing in branch offices and is overworked elsewhere. It seems from a practical point of view to work better in a separate organization.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Do the operations of RoyNat come under the inspection of the Inspector General of Banks?

Mr. McLAUGHLIN: No.

The CHAIRMAN: Does anyone inspect it?

Mr. McLAUGHLIN: It is audited.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): By whom?

Mr. McLAUGHLIN: By Peat, Marwick, Mitchell & Co.

RoyNat is an ordinary company under the Canadian Companies Act.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It does not come under the inspection of the banks? Thank you, that is all just now.

The CHAIRMAN: I now recognize Mr. Monteith.

Mr. MONTEITH: Mr. Chairman, I have just a couple of questions. On the balance sheet of RoyNat there are two liabilities: \$60 million, Secured Notes and \$14.7 million, Debentures Series A. Are these sold to the public?

Mr. McLAUGHLIN: Yes, they are.

Mr. MONTEITH: I have one other question. Mr. Powell, you mentioned that the loans are between \$25,000 and \$1 million, approximately with one having gone to \$2 million, and so on. You said you get 70 per cent of your inquiries through branches, and this sort of thing. Once you get an inquiry what are the various steps you take before deciding whether or not a company is a good risk. I am thinking of a new company—somebody with a new idea.

Mr. POWELL: Well, first of all, we have a relatively simplified procedure and if someone wants to get some money from us they complete a standard document which we call the "inquiry form". That form is sent into us either through any one of the 1,700 branches of the banks, sometimes directly or through the trust companies. When we see this preliminary form we can pretty well tell whether or not that particular proposition might fit our way of doing business. And we then get an application form completed which is rather a lengthy document, something like the prospectus would be for an issue of securities. If we are looking at a completely new business, however, it is more intricate obviously because you have to have a market study, you have to have a feasibility report which is generally prepared by the people who are coming to you for the money and after assessing the capital they intend to put in it, what the product is, what you think the success will be or will not be of it, you make your decision on that. Our decisions on loans are made through an investment committee which is used for decisions on all of our loans. Those over a certain amount are referred to our executive committee. Does that answer your question?

Mr. MONTEITH: Yes. Just to follow up Mr. Lambert's earlier question, I am afraid I did not get the exact date of when you became aware, Mr. McLaughlin, that RoyNat was apparently being discriminated against in the present bill.

Mr. McLAUGHLIN: When we saw the bill.

Mr. MONTEITH: That is all, Mr. Chairman.

(Translation)

The CHAIRMAN: Next Dr. McLean, followed by Mr. Laflamme.

(English)

Mr. McLEAN (*Charlotte*): I have a couple of questions. If RoyNat is exempted under the bill would this lead to other companies asking for the same exemption and would you have any objection to the other companies being exempted the same as RoyNat?

Mr. McLAUGHLIN: Mr. McLean, the answer to that is no. I can speak only for RoyNat. I cannot make a plea for such other companies as may be comparable to it—Kinross has been mentioned—because I am not in a position to do so. But I would have no objection; in fact, I think, perhaps there are some that are filling



what we think is a gap which would continue and undoubtedly they should be included in any exemption if an exemption is granted for RoyNat.

Mr. McLEAN (*Charlotte*): You borrow and lend on long-terms at RoyNat?

Mr. McLAUGHLIN: That is correct. You see there are three reasons for the formation of RoyNat. Two of them were quite subsidiary reasons. One of the subsidiary reasons was the fact that at the time RoyNat started, the banks themselves could not charge more than 6 per cent and the going rate, the Industrial Development Bank rate was more than 6 per cent. The second was that the banks could not take mortgage security, but if this bill goes through they can. These were very subsidiary reasons. The principal reason for starting RoyNat was the fact that it is only proper when you lend long you should borrow long and the banks have short-term deposits. That reason, of course, will continue to exist.

Mr. McLEAN (*Charlotte*): You say the Industrial Development Bank charges more than 6 per cent?

Mr. McLAUGHLIN: Oh, yes, indeed. They charge  $8\frac{1}{2}$  per cent or more. Seven and one half or  $8\frac{1}{2}$  per cent. They do not publish their rates but—

Mr. McLEAN (*Charlotte*): It is a government institution, is it not?

Mr. McLAUGHLIN: It is a subsidiary of the Bank of Canada.

Mr. McLEAN (*Charlotte*): Would the RoyNat make larger loans than the Industrial Development Bank?

Mr. McLAUGHLIN: I do not know what is the size of the Industrial Development Bank loans but as I indicated before it is not the purpose of RoyNat to make loans, where the size is such that the company in the ordinary course through an investment dealer can have a public issue. It is to fill the gap. It is very expensive to have a public bond issue for \$250,000, in fact, it is impossible. You cannot have an exact cut off but more or less a million dollars is where we think the cut off should be. As you can see there are only a handful of loans above a million dollars.

Mr. McLEAN (*Charlotte*): I was thinking that you might be filling a gap that the Industrial Development Bank would not be filling.

Mr. McLAUGHLIN: The Industrial Development Bank is supposed to be a lender of last resort, if you like, a government institution. I would like to think that RoyNat is perhaps a private industrial development bank. There is a need for it.

Mr. McLEAN (*Charlotte*): The Industrial Development Bank base their interest rates on the risk.

Mr. McLAUGHLIN: That is correct, the risk and general interest rates.

Mr. McLEAN (*Charlotte*): The banks at the present time are not allowed to base their interest rates on risk.

Mr. McLAUGHLIN: Unfortunately, that is true.

Mr. McLEAN (*Charlotte*): I notice that RoyNat has paid no dividends, except preferred.

Mr. McLAUGHLIN: The reason for that is the more surplus—and it is not very large yet—that can be accumulated by leaving the profits—modest as we are in that—the greater is its long-term borrowing power. Of course, that is

another reason why we hope that the shares do not have to be divested. When we are in the public hands some dividend would have to be paid. The five shareholders, as it is now, are prepared to take a long view and wait. If dividends were paid the capital and the surplus would be less than it is now and that gives less leverage. They would not be able to borrow as much long and therefore they could not lend as much.

Mr. McLEAN (*Charlotte*): That is what I have been thinking, that the banks and trust companies having ownership were in a better condition to wait for dividends than the general public would be.

Mr. McLAUGHLIN: The profits have been reasonably satisfactory but as indicated in the brief we could have made more money by investing the same amount in Government of Canada bonds. We take the long view that this is going to pay us a reasonable dividend and we are prepared to wait because we think it is doing the country some good in the meantime.

Mr. McLEAN (*Charlotte*): Thank you.

The CHAIRMAN: Now, Mr. Laflamme.

Mr. LAFLAMME: Mr. Chairman, I will pass for the moment.

The CHAIRMAN: Then we have Mr. Flemming followed by Mr. Gilbert.

Mr. FLEMMING: Mr. Chairman, my question to Mr. McLaughlin is in relation to the ownership of the shares. Did those who were responsible for the formation of RoyNat have any idea there existed in the minds of any minister of finance with whom they may have been discussing the matter or any officials that there would be a limit of 10 per cent placed on the ownership that any chartered bank could have in such an institution.

Mr. McLAUGHLIN: None, whatsoever.

Mr. FLEMMING: Had you known that there did exist such an idea, Mr. McLaughlin, would it have changed your thinking about the formation with the bank itself.

Mr. McLAUGHLIN: Had that limitation of 10 per cent been in effect RoyNat would not have been formed—could not have been formed.

Mr. FLEMMING: Thank you, that is all.

Mr. GILBERT: Mr. McLaughlin, are there directors and officers of the bank who are also directors and officers of the trust companies. In other words, are they interlocking?

Mr. McLAUGHLIN: Between RoyNat and the banks?

Mr. GILBERT: Yes.

Mr. McLAUGHLIN: Mr. Davignon, the chairman of the board of RoyNat was an assistant general manager of the Banque Canadienne Nationale. He has since retired from that post but continues. Mr. Powell used to be a deputy general manager of the Royal Bank of Canada. He is full time and chief executive officer. Mr. Coleman is the chief general manager of the Royal Bank of Canada and represents the Royal Bank's holdings of RoyNat. Mr. Faribault, as you know, is president of the Trust Generale. Mr. Hébert is the president of the Banque Canadienne Nationale. Mr. Hodgson represents the Montreal Trust. Mr. Knight died three weeks ago. He was a chartered accountant and had no connection with

any bank. The man who did the survey which made possible RoyNat, Mr. Treleaven, represents the Canada Turst Company.

Mr. GILBERT: Mr. McLaughlin, would you agree with me that the Porter Commission set forth the principle that it was not a wise thing to have concentration of power and this may be the reason why the government is asking for the divesting of a certain share of the interest of the banks in these companies.

Mr. McLAUGHLIN: It may be; I do not know what the reason is. I do not think there is a concentration of power. None of the five shareholders runs RoyNat. I have been in their offices once just to see it. The only suggestion I made when RoyNat was being formed, which I think has been followed, is that when it set its offices up across the country under no circumstance would I hope that it would have its office in the same building as any of the five shareholders, to maintain its independence. RoyNat has turned down loans that managers of both branches had submitted to it. It operates quite independently. There is no concentration of power.

Mr. GILBERT: Would you say that there is a trend with regard to the concentration of power by RoyNat and Kinross and Triarch—there are about five of them. Would you say that is a trend?

Mr. McLAUGHLIN: I do not think so. I cannot speak for the others but if I may be lighthearted for a moment—

The CHAIRMAN: It is always permissible to be lighthearted for a moment.

Mr. McLAUGHLIN: We think RoyNat was a wonderful idea. We are embarrassed that we did not get the idea sooner. The Industrial Development Bank had existed for some years doing this very job. Why we did not see that we could do it too as a private organization sooner I do not know. But, it is like everything else, when you get a good idea you wonder why you did not get it sooner. All we are doing privately is what the Industrial Development Bank is doing as a subsidiary of the Bank of Canada. There was an obvious gap there which—well, just had not been filled.

Mr. GILBERT: I notice that you ask for an amendment following the words "The Export Finance Bank".

Mr. McLAUGHLIN: Well, it seemed to me that was the logical place to put it in. If you want to put it in any place else I have no objection as long as it is in.

Mr. GILBERT: Well, I am just going to direct our attention to clause 76(8) and ask you to look at subparagraph (C). It is the large (C) of paragraph (a). In this paragraph (a) it says:

(a) "bank service corporation"

And subparagraph (C) says:

(C) a corporation engaging in the business of providing a service incidental or ancillary to, or used in the carrying on of, the business of the bank or of a corporation referred to in clause (A) or (B).  
Do you think that RoyNat falls within that exemption?

Mr. McLAUGHLIN: When I first read that I thought that it did but legal advice has since indicated that that is not the intention. I am told this covers real estate companies owning branches or perhaps the company that washes the



windows in the branch—it does not cover RoyNat. If it did, I would not be here today. You can ask Mr. Elderkin.

The CHAIRMAN: Mr. Elderkin, if we can just call you in at this point. This may have been dealt with at our explanatory sessions before we began our public hearings; but, as far as the views of the legal advisers of the government are concerned, what is the significance of this section.

Mr. C. F. ELDERKIN (*Inspector General of Banks, Department of Finance*): RoyNat would not fall within this section. Mr. Chairman, may I add the counsel for the Canadian Bankers' Association, also in a previous testimony here said that in his opinion RoyNat did not fall within subclause (7).

Mr. GILBERT: I think Mr. Elderkin is correct. I think I recall asking him that and he gave the same answer. I was just testing Mr. McLaughlin on his idea. Mr. Chairman, those are all the questions I have to ask at the moment.

Mr. McLAUGHLIN: I have great respect for the Inspector General's decisions.

The CHAIRMAN: I hope so. Mr. McLaughlin, I wonder if you could give us some information on the association of the owners of RoyNat between themselves. For example, the Royal Bank of Canada is one of the owners of RoyNat. Are there directors in common between the Royal Bank of Canada and the Montreal Trust Company?

Mr. McLAUGHLIN: There are directors in common but no common ownership. In other words, there are individuals who are directors of the Royal Bank of Canada who are also directors of the Montreal Trust Company. The Royal Bank of Canada does not directly or indirectly own a single share of the Montreal Trust Company.

The CHAIRMAN: What about the Royal Bank of Canada and the Canada Trust Company?

Mr. McLAUGHLIN: There are common directors but no share ownership.

(Translation)

The CHAIRMAN: Mr. Hébert could answer the following questions on relations between the Banque Canadienne Nationale and the Trust Général du Canada?

Mr. HÉBERT: There are none.

The CHAIRMAN: Are there common directorships?

Mr. HÉBERT: Yes, there are, the directors of the Banque Canadienne Nationale are also directors of the Trust company.

(English)

The CHAIRMAN: Mr. McLaughlin, I wonder if you would take a look at page 7 of your very helpful brief. With respect to clause (a), if for the sake of argument the proposals of the government became law it would still be possible for the institutions in question to retain a much more limited interest in RoyNat.

Mr. McLAUGHLIN: Ten per cent each.

The CHAIRMAN: Yes. This information would be available to the public?

Mr. McLAUGHLIN: That is correct.

The CHAIRMAN: Do you feel that there would not still be some strengthening of RoyNat's position in the mind of the public, knowing that information was there, that link was there?

Mr. McLAUGHLIN: Mr. Chairman, it would be better than if there was no link at all but at the moment between the two banks it is 75 per cent. I think in the mind of the public there is a great difference between a 75 per cent sponsorship and a 20 per cent sponsorship.

The CHAIRMAN: You do not think that RoyNat has become so sufficiently established by now that it could stand on its own feet with respect to the market.

Mr. McLAUGHLIN: It could stand on its own feet but at a higher price. I am satisfied that the sponsorship—there is no guarantee—this is a separate company—but the sponsorship of the banks I am satisfied has enabled RoyNat to raise its long-term funds from the public at an eighth or a quarter of one per cent better than it could without bank sponsorship. I do not think that 10 per cent each is sufficient bank sponsorship to maintain that privileged spread in the rates.

The CHAIRMAN: What about the effect on the minds of the purchasers of RoyNat's success?

Mr. McLAUGHLIN: Well, those are the ones you have to ask. After all, they are the ones who buy the security.

The CHAIRMAN: You are suggesting that RoyNat's own success is not sufficient to justify the same favourable reaction of the market that you have now?

Mr. McLAUGHLIN: RoyNat has not gone long enough yet to be eligible for investment by insurance companies. I think it has another year to go. It is five years you have to operate to be eligible for insurance companies. That is a hampering factor right now. If you like, the moral backing of the banks is worth a quarter of one per cent. As I said before, I do not think that that exists. We would not have the same interest with a 10 per cent interest—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. McLaughlin, do you think if the Royal Bank of Canada and the Banque Canadienne Nationale were obliged to divest themselves of everything but the 10 per cent permitted in the bill and their remaining shares were taken up by the Montreal Trust Company, the Canada Trust Company and the General Trust Company of Canada that there would not be a maintenance of public confidence? There is a fairly clear recognition in the public mind of, shall we say, links between the Montreal Trust and the Royal Bank and other type companies and the banks.

Mr. McLAUGHLIN: Mr. Cameron, there are directorship links but there is no investment link and if another section of Bill No. C-222 goes through those directorship links will be severed, too. I would think that the investment is probably—I do not know whether the three trust companies legally could take it up. They have some limit on their investment. But, even if they could, I would think that the investment would be fairly sizeable for them—they are not the size of the banks. What I fear is if the two banks are forced to dispose of the shares, there are a number of ways in which it could be done. One of them is to have it listed on the stock exchange and make an issue. Then, there is 75 per cent floating around. Someone else—who knows who it would be—who it would be is beyond anyone's control—would only have to buy 50 per cent of it. We may not

even want to keep our 10 per cent if it gets in, what you might call, unfriendly hands. It is beyond our control what will happen to it.

Mr. GRÉGOIRE: Mr. McLaughlin, I would like to ask you this question. Would the Royal Bank of Canada be interested in keeping its 10 per cent share if that clause were enacted?

Mr. McLAUGHLIN: The answer is it would all depend on whether or not someone acquired quite legally majority control and who that someone was. That someone might be—if I can use the phrase—“unfriendly hands”, meaning from a competitive point of view. We are not going to have our 10 per cent. We are not going to distribute, through our branches to help someone who is competing with us.

The CHAIRMAN: Are you not competing with the Banque Canadienne Nationale?

Mr. McLAUGHLIN: Ah, I did not mean it that way.

Mr. GRÉGOIRE: May I ask a question?

(Translation)

A question, Mr. Hébert. Would the Banque Canadienne Nationale get rid of its shares in the event of the case just mentioned arising?

Mr. HÉBERT: As mentioned by Mr. McLaughlin, it is certain that if the shares that we hold were to fall into hands that were not friendly towards us, I think that we would be ready to get rid of our shares.

The CHAIRMAN: A personal question?

(English)

Mr. LAFLAMME: Mr. Chairman, I have a supplementary question. I think this is the main point, the effect of the application of clause 76 on the survival of RoyNat itself. Mr. McLaughlin, will the life of RoyNat be in danger if this clause applies? I would like you to clear this up in my mind.

Mr. McLAUGHLIN: First of all, if it is divorced from its shareholder banks I think its cost of raising money will go up and it has to operate at a profit or it serves no useful purpose. Therefore, what it charges will have to go up. Second, I think RoyNat has a great future. I think over the years it can lend much more than it is lending now. There is a demand; there is a gap. But, to do so, it has to borrow money. However, there is a limit on what it can borrow in relation to its capital, and it is much easier for the five shareholders to put in additional capital than it is to raise it from the public. Furthermore, if it gets in the public's hands, and has to pay a dividend, that reduces the amount which is left over which is a base for raising additional capital and it cannot grow as fast. I do not think it can serve the public as well under any circumstances as it is now. That is not to say it cannot serve them in some way but I think it will be more expensive, in a smaller way, and it just will not be as good.

(Translation)

The CHAIRMAN: Mr. More. One moment, Mr. More has indicated that he has questions to put, Mr. More.

(English)

Mr. MORE (Regina City): Mr. McLaughlin, I just have two questions. RoyNat is not subject to the Bank Act; therefore, public offering of your holdings could mean foreign take-over, could it not?



Mr. McLAUGHLIN: It could. There is nothing to prevent it. If we offered it, such as on the stock exchange, then it is beyond out control who buys it.

Mr. MORE (*Regina City*): Would this not be necessary if you are forced to divest?

Mr. McLAUGHLIN: Yes. That is one of the ways, but I do not know how we would do it. The logical way I should think would be to list it on the stock exchange, have a secondary offering, and then anyone can buy it. There is nothing to prevent foreign take-over and that is what I meant when I said in "unfriendly hands" more than anything else.

Mr. MORE (*Regina City*): I think that clears that. Your present investment guarantees Canadian ownership.

Mr. McLAUGHLIN: Absolutely.

Mr. MORE (*Regina City*): The other question is this: Do you look forward to qualifying for insurance company investment. Will that increase the growth possibilities of RoyNat operations?

Mr. McLAUGHLIN: It increases the sources from which they can borrow long.

Mr. MORE (*Regina City*): This would be a source?

Mr. McLAUGHLIN: That is correct.

(*Translation*)

The CHAIRMAN: Mr. Grégoire.

Mr. GRÉGOIRE: Mr. McLaughlin, if the other chartered banks were to acquire 10 per cent each up to the 55 per cent and then you had to get rid of 10 per cent of these RoyNat shares, would you consider those shares as being in competitive hands? Would that be competition?

(*English*)

Mr. McLAUGHLIN: It would be partially competitive if the 10 per cent went into each of the other banks. I do not think that would happen, Mr. Grégoire, for some of the other banks have interests in some of the like companies. I do not think you would want to invest in two companies doing this. We thought that this was a happy combination of the Banque Canadienne Nationale and the Royal Bank of Canada competing in other ways to get together on this subject that we could not do independently. I am surprised—although pleased—that the other banks have not moved sooner to form similar companies in partnership to compete with us. I thought that would be the next step, that two months after we had this good idea there would be other competition, but it has not happened in the same way. Some of them have bought into other existing companies. I cannot speak for the other banks but I would doubt, if having a small interest in a smaller but somewhat similar company, they would want to have an interest in two.

(*Translation*)

Mr. HÉBERT: Marriage is always better when there are two, than when there are three.

The CHAIRMAN: That is a question of opinion is it not?

(English)

This is the Finance Committee not the Committee on Justice and Legal Affairs.

(Translation)

I would like to put an additional question because some thoughts arose in my mind.

Mr. GRÉGOIRE: Another supplementary question. Mr. McLaughlin, in view of the fact that the share capital is ten million, that the trust companies already have 25 per cent of the shares, that is \$2,500,000 and your two banks are authorized to have \$2,000,000 that means with \$5,500,000 someone could control the RoyNat company, could they not?

(English)

Mr. McLAUGHLIN: Mr. Grégoire, the Banque Canadienne Nationale and ourselves could, if we got together, control RoyNat but neither one of us independently does.

(Translation)

Mr. GRÉGOIRE: But with the provisions of the Act if your two banks were obliged to sell 55 per cent of their shares that would mean \$5,500,000, and a third party that could then control RoyNat?

(English)

Mr. McLAUGHLIN: That is correct. If the shares had to be disposed of it is legally possible for someone to step in and buy 55 per cent and control the company.

Mr. LAFLAMME: But they would be bought at the higher price.

Mr. McLAUGHLIN: Well, at a higher price, yes. In other words, you are suggesting that there might be a profit on the sale of the shares to the bank. That is possible but that is not the type of profit we are looking for. That is not why we formed the company.

The CHAIRMAN: Mr. McLaughlin, I was very interested in your comments on the effect of disposition of shares by yourself and your associates on the method of operation of RoyNat. I am speaking theoretically—if you would only be able to have the interest referred to in the Bank Act why would the public be deprived of the ready access to information concerning RoyNat's facilities. Could you not by agreement make the same type of arrangements you have now?

Mr. McLAUGHLIN: Mr. Chairman, we could but I get back to this phrase "unfriendly hands". It might not be in our interest to aid a foreign competitor. I do not know who may buy this 55 per cent and it may not be in the interest of the shareholders. We might be better off to get rid of our 10 per cent and say goodbye to RoyNat.

The CHAIRMAN: But if the other purchasers were not considered unfriendly in the sense you would use the term, then would you agree that there is nothing that would flow automatically from the terms of the law which would prevent RoyNat from having the same access to your facilities as it does now.

Mr. McLAUGHLIN: There is nothing to prevent it, that is true. I doubt whether it would work that way but there is nothing legally to prevent it.

The CHAIRMAN: The reason I asked this is that when you answered my previous questions about the links between yourself and the other sponsors, you pointed out that there is only a link through the directorate.

Mr. McLAUGHLIN: That is correct.

The CHAIRMAN: I gather these links have been quite useful to yourself and your associates with respect to exchange of information, not about RoyNat but trust company business and banking business and reference to clients.

Mr. McLAUGHLIN: They certainly were in the days when trust companies and the banking business was complementary. We could not do trust company business and the trust companies did not—years ago—do bank business.

The CHAIRMAN: What I am driving at, sir, is that it is not necessary to have ownership to have a very useful relationship.

Mr. McLAUGHLIN: That is true.

The CHAIRMAN: This is evidenced by the relationship you already have between banks and trust companies.

Mr. McLAUGHLIN: That is true.

The CHAIRMAN: With respect to the present type of operation of RoyNat; first of all, have you calculated the amount of debentures which the chartered banks, or your bank alone, could issue if the provisions of the bank bill were adopted into law.

Mr. McLAUGHLIN: Yes, ultimately \$160 million.

The CHAIRMAN: You refer to your own institution?

Mr. McLAUGHLIN: Yes, roughly.

The CHAIRMAN: This is a new lending that you could not do—

Mr. McLAUGHLIN: It is a new source of money.

The CHAIRMAN: A new source of money. Let us assume the market wishes to purchase—

Mr. McLAUGHLIN: In due course, when it builds up over five years. It is 50 per cent of our capital in certain areas.

The CHAIRMAN: One hundred and sixty million dollars; that is quite a substantial amount.

Mr. McLAUGHLIN: Yes, it is except that the amount we can lend in mortgages is substantially higher than that. There seems to be a demand for mortgages. As I said earlier this morning, I think most banks have mentally allocated the debentures to mortgages.

The CHAIRMAN: And the amount of mortgages.

Mr. McLAUGHLIN: Residential mortgages.

The CHAIRMAN: The reason I asked this question was that it was my understanding from the bankers' association when they were here that they would use at least some of the opportunities to lend mortgage for term lending to business.



Mr. McLAUGHLIN: I can only speak for the Royal Bank of Canada. I do not think I would want to do it that way.

The CHAIRMAN: You would not want to do it that way? This may come as a surprise to some potential or actual commercial customers who had hoped the mortgage provisions would enable you to lend them money for their commercial purposes under certain terms.

Mr. McLAUGHLIN: There may be some of that but I think—

The CHAIRMAN: But there will not be any with your bank?

Mr. McLAUGHLIN: No, I do not say that there will not be any. I would not like to make a commitment like that. Mentally, I think most of the debenture money will go into residential mortgages.

The CHAIRMAN: What about your colleague banks?

Mr. McLAUGHLIN: You will have to ask them.

The CHAIRMAN: Perhaps we should at some later—

Mr. LAFLAMME: They will have the power to do so.

Mr. McLAUGHLIN: They will have the power. We will make some commercial mortgages but what is needed at the moment, I think, when we can get the money, is residential mortgages more than commercial mortgages. There are markets for those.

Mr. LAFLAMME: I am sorry, Mr. Chairman. With the application of this new bill the banks will be able to fill the gap, at least part of the gap, that you have said RoyNat has filled.

Mr. McLAUGHLIN: Yes, we will be able to fill the gap, but do not forget that to be sound one should not lend too much long unless one borrows long. The amount of long borrowing by way of debenture is considerably less than the amount of long term lending one is allowed to do by way of residential mortgages. If there is a big demand for residential mortgages—over the years ahead, not tomorrow, but over the years ahead I would think it would be largely used up by the amount of debentures. Then you just sit back and make a judgment. Are we going to do less residential mortgages and more RoyNat type of business. Well, I say, here is the problem solved. RoyNat exists; you do not have to worry about this; it can do it. It raises its money independently and that leaves us more for residential.

The CHAIRMAN: Your existing commercial customers who have been waiting for the opportunity to borrow on security of mortgage should not get too enthusiastic.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): They would be referred to RoyNat.

Mr. McLAUGHLIN: They are now in the size that RoyNat handles it. I do not think the lineup is as nearly as long—if there is a lineup at all—as those wanting residential mortgages.

The CHAIRMAN: I think I would agree with you. A further point here. If this very interesting point you made about debenture borrowing could be overcome,

why could not the banks have the same type of specialized organization as RoyNat has? What is to stop them?

Mr. McLAUGHLIN: Mr. Chairman, that is an excellent question. I tried to explain before the banks have operated on the basis of trying to have the same facilities at every branch. Maybe in the future we will depart from that. Perhaps if you want one type of loan you can get it at any branch. If you want a special type of loan you have to go to one branch per city. But at the moment we do not operate that way. This is a specialized business. It has engineers; it has accountants; it has staff that the banks do not have.

The CHAIRMAN: But there is nothing to prevent the—

Mr. McLAUGHLIN: There is nothing to prevent it except from a practical operating point of view it works better to have it in a smaller organization like this where it is concentrated.

The CHAIRMAN: Now, with respect to Mr. More's very useful point, are you aware of a particular foreign interest who would like to get a hold of RoyNat?

Mr. McLAUGHLIN: No.

The CHAIRMAN: Can you give us any names?

Mr. McLAUGHLIN: No, I cannot say. All I am saying is that there is nothing legally to prevent a foreign interest from buying it if we have to divorce ourselves. I know of no one. I hope that no one has an opportunity. I hope that there is some amendment to the bill so that it is not possible for them to do so. But if 75 per cent of it is made available to the general public in some manner before 1971, there is at least nothing to prevent this. I do not think that they will, but I just wanted to point out it is possible.

The CHAIRMAN: I have one final point. You mentioned the possibility of RoyNat under these provisions falling into the hands of possible banking competitors.

Mr. McLAUGHLIN: No I said "unfriendly hands." I think someone else raised the question.

The CHAIRMAN: You mean you are not concerned about other banks acquiring the interest if these provisions are adopted into law?

Mr. McLAUGHLIN: I can only speak for myself. There are one or two other banks that have interest in somewhat similar smaller and lesser known companies. If they have to put the excess over 10 per cent on the market, personally, I would not be interested at all in buying them. I doubt whether any other bank would be interested in RoyNat. This has become known as a Banque Canadienne Nationale—Royal Bank sponsorship and the competitive situation is such that I doubt whether another bank would want to buy into it. I cannot speak for them; I can only speak for myself. I would not want to buy into anything that they had to divest themselves of, of a similar nature.

The CHAIRMAN: Why? Is that a form of *noblesse oblige*?

Mr. McLAUGHLIN: No. Not at all. I just do not think it would accomplish anything.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): May I ask a supplementary at this point? What would be your attitude, Mr. McLaughlin, if you were

faced with this problem, or finally are faced with this problem, of divesting yourself of the interest in RoyNat? Would it not be possible for you and your partners in this operation to approach the other chartered banks and suggest the setting up of a new corporation on the style of RoyNat that would involve all the chartered banks? Would you then be in an equally favourable position?

Mr. McLAUGHLIN: We might have to wait awhile, Mr. Cameron. I had given some thoughts to that myself although I did not tell anyone about it. My arithmetic indicated it was impossible because there are only eight chartered banks and eight times 10 per cent is 80 per cent.

Mr. GRÉGOIRE: Plus the trust companies—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): There are two trust companies.

Mr. GRÉGOIRE: There are ten chartered banks now.

Mr. McLAUGHLIN: They are close to it, but they are not in operation.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Do you not think, Mr. McLaughlin, in those circumstances if such a new organization was formed, with the added resources of the other banks, that the position of your bank would be as favourable as it is now in RoyNat. You would have your share of the expanded organization.

Mr. McLAUGHLIN: RoyNat has a certain advantage to the banks that own it now which would disappear. As has been indicated, by no means are all loans made to existing clients of the two banks. Quite a few of them are made to clients of other banks. If they want to remain clients of the other banks they are perfectly free to do so. But, there is always the chance that we might get one or two accounts out of this. There is a competitive advantage which would not exist if all banks owned it. You would not have the same enthusiasm for it.

The CHAIRMAN: In other words, does this flow from this: Are you and the Banque Canadienne Nationale less competitive between yourselves than you are with the other banks?

Mr. McLAUGHLIN: No, sir. We certainly are not.

The CHAIRMAN: Next we have Mr. Grégoire and then Mr. Lambert.

(*Translation*)

Mr. GRÉGOIRE: You asked that RoyNat be exempt from Section 76(1) Bill C-222. Do you ask for this exemption because you are in existence already and because there would be some retroactive effect that would endanger your interest? Or are you asking for the exception for RoyNat because you think the other chartered banks should be exempted in the future and might equally set up agencies like RoyNat?

(*English*)

Mr. McLAUGHLIN: I am asking for RoyNat because it is the only one I can ask for. I would have no objection if instead of putting this in as an exemption for RoyNat there was another clause put in here which would make it possible for other organizations such as RoyNat to be formed by other chartered banks. I am not trying to be selfish and keep this for the two banks. There is a gap. I do not know if RoyNat can fill it all and it would not bother me a bit if two other



banks and three other trust companies got together and formed a RoyNat No. 2, or whatever they want to call it. I would not object to that at all. I would be quite happy if a provision could be put in this bill which would not only exempt RoyNat but exempt any other gap filling organization that private initiative wanted to start up where there is a gap.

*(Translation)*

Mr. GRÉGOIRE: We are speaking of organizations controlled by chartered banks, so we would not take into account only the past but the future. The exemption would apply to any banks that wanted to set up a similar organization, subsidiary companies extending industrial or commercial loans. Is that the type of exemption you want? Do you want exemptions to be granted to corporations extending this type of loan as RoyNat does?

*(English)*

Mr. McLAUGHLIN: I would be quite happy if there could be an exemption if a bank wanted to operate through a subsidiary rather than directly.

*(Translation)*

Mr. GRÉGOIRE: Would this exemption be limited to the industrial field, or do you think this could also pertain to other fields? Let us suppose that within one year, the Royal Bank of Canada and the Banque Canadienne Nationale, would like to create another RoyNat but only for mortgages. Do you think this exemption would also apply to these other fields of loans?

*(English)*

Mr. McLAUGHLIN: If two banks wanted to get together and form a company to make mortgage loans which is another way of raising long-term money, apart from debentures, I think that should be exempted too.

*(Translation)*

Mr. GRÉGOIRE: In other words it is not only the question of RoyNat. It is the whole item 76 of the Bill?

*(English)*

Mr. McLAUGHLIN: That is correct. I am here specifically because of RoyNat making a plea for that, but also plea for the principle which is bigger than RoyNat.

*(Translation)*

Mr. GRÉGOIRE: Do you think that for the good of Canadian people and the Canadian economy, item 76 should be deleted completely?

*(English)*

Mr. McLAUGHLIN: I think no harm has been done by the fact that clause 76 was not in it before. I think I know what the intention is and, in principle, if I am correct in my assumption, I cannot disagree with it; that is, that banks are not formed to obtain control of International Nickel or Canadian Pacific Railway. But this is sometimes a case of throwing the baby out with the bath.

There are other situations where I think it might be harmful. More than 10 per cent but less than control is often good and particularly when it does not involve a major company. Let me give you an example which is ancient history now. A client of ours some time ago sold his products through a small com-

pany—he made some loans to it—and this company was going to go into bankruptcy. He did not want that to happen and he offered to buy out the company. For technical reasons he did not want this to show as a subsidiary of his and he asked us—he was a valued client—if we would temporarily take 50 per cent of this company. It was a service that we could render but it was 50 per cent. The amount involved was \$5,000. Now, we could not have serviced a good client—if this clause must be in I would like to make a plea that, apart from RoyNat, you make an exemption of up to say \$250,000 or \$500,000. I do not think that defeats what I see as the purpose of this clause, if it is, that you are not going out to try and control, as I say, International Nickel. There are often situations where at least on a temporary basis one has had more than 10 per cent of a private company. It is harmful if you cannot because you cannot help a client. Five thousand dollars is not going to change the economy.

(Translation)

Mr. GRÉGOIRE: I wonder whether sub-clause 4 of section 76 does not give you that possibility, by making clear that “the bank may acquire shares above the maximum authorized under this section, but must sell this surplus stock or dispose of it within a period of two years reckoned from the date of acquisition.”

I wonder whether this sub-clause does not allow you to do what you have just mentioned?

(English)

Mr. McLAUGHLIN: It does if the transaction can be concluded within two years but banking is a patient business and often we have to hang on to things for a lot longer than two years, so we would be precluded.

(Translation)

Mr. GRÉGOIRE: Paragraph 5 says that the Minister can postpone the deadline beyond two years.

(English)

Mr. McLAUGHLIN: That gives you a total of four years. I do not know whether the minister would do it, he may. That gives you a total of four years, and four years are often a relatively short time.

(Translation)

Mr. GRÉGOIRE: Mr. McLaughlin or Mr. Powell, with regard to the operations of RoyNat, do you have the same rate for any business?

(English)

Mr. POWELL: We have a prime rate. Our prime rate today is 8 3/4 per cent and we move up by one per cent depending upon the type of transaction we are financing. This depends on the nature of the business, the security and—

(Translation)

Mr. GRÉGOIRE: What is the kind of transaction or industry which commands the highest rate of interest?

(English)

Mr. POWELL: There is no set industry that would be always entitled to the lowest rate or the highest rate. It depends upon the type of operation that it is and also is based on the type of security. In other words, if you are financing against trucks and equipment, and so forth, the rate is generally the highest for

that type of financing. But if you are financing the erection of a new plant or a business or the acquisition of machinery and equipment, provided the basic security values are right, then they would be entitled to the lowest rate which would also be supported, of course, by their cash flow or the profits they make, in order to service the debt.

*(Translation)*

Mr. GRÉGOIRE: Now, if you compare the interest rate charged by RoyNat with the interest rate charged by the Industrial Expansion Bank, including charges which can increase that absolute interest rate, I wonder whether the rates are comparable or whether there is a substantial difference, and to whose advantage is the difference?

*(English)*

Mr. POWELL: The difference is approximately—I am taking it on the basis of the Industrial Development Bank loaning at  $8\frac{1}{2}$  per cent or more. I do not know exactly what their rates are today. Our prime rate is  $8\frac{3}{4}$  per cent but I think if you took it out over the average it probably would be about three quarters to one per cent higher than the Industrial Development Bank.

Mr. GILBERT: Mr. Chairman, I have a supplementary question. What percentage of your own applications are rejected, Mr. Powell, just the approximate number?

Mr. POWELL: Since we started in business, up to October 31, of all of the inquiries we have received, 24 per cent of all of them have resulted in accepted transactions.

Mr. GILBERT: That means 76 per cent are rejected?

Mr. POWELL: Seventy-six per cent are inquiry standards. That is not applications. The inquiry is the first document. After the first inquiry is looked at it would get into the application form if the type of transaction presented to us fits our form of doing business.

Mr. GILBERT: Are you saying that 24 per cent of all inquiries are accepted.

Mr. POWELL: Twenty-four per cent of all inquiries are accepted.

Mr. GILBERT: Twenty-four per cent are accepted. Let us get to the next stage then. What percentage of applications are accepted?

Mr. POWELL: The applications come out of the inquiry and by the time it gets into the application form—unfortunately, I cannot give you a straight answer on that. If you wanted to work it on the basis of those that get into application my guess is roughly 36 per cent.

Mr. GILBERT: Thirty-six per cent are accepted.

Mr. POWELL: Yes, 36 per cent are accepted.

*(Translation)*

The CHAIRMAN: Have you any other questions to pose, Mr. Laflamme.

Mr. LAFLAMME: I would like to put another question to Mr. Hébert, Mr. Chairman, if Mr. Lambert will allow.

Mr. LAMBERT: My questions do not concern RoyNat, so I will yield the floor.



The CHAIRMAN: I have the feeling the Committee is almost through with the brief. Members are finishing up.

Mr. CLERMONT: Mr. Chairman, I wonder whether the Committee would like to print the submission as an annex to our proceedings; because Mr. McLaughlin gave us a summary. I would like to know whether we shall print that.

The CHAIRMAN: Thank you very much for asking. I do believe we shall. The clerk has just told me that we have a motion for the printing of this submission. It is not necessary to have a motion each time. We have a motion covering all submissions.

Mr. LAFLAMME: When you lend money to an industry, do you take out a deed of trust or just a mortgage?

Mr. HÉBERT: Are you talking of the bank?

Mr. LAFLAMME: No, of RoyNat.

Mr. HÉBERT: It is RoyNat—

Mr. LAFLAMME: So, you have a trust act?

Mr. HÉBERT: Yes.

Mr. CLERMONT: Mr. Powell, what to you mean by “amount to repay on debentures”? In 1966, \$900,000 and in 1967 \$1,200,000.

(English)

Not \$12,000 — \$1.2 million.

Mr. POWELL: Well, those are commitments we have on our own issues of security in which there are purchase fund covenants which cause us to have to buy in some of our own debentures and/or secured notes each year. Last year it was \$900,000 and this coming fiscal year it will be \$1.2 million.

The CHAIRMAN: What percentage of your borrowing—perhaps I could make a computation myself—what percentage of your total borrowing to date could be described as short-term.

Mr. POWELL: Just what you see on the balance sheet as of April 30, 1965. It was \$10,200,000 at that date which shortly after this was refinanced by another issue of secured notes.

The CHAIRMAN: So it disappeared. Thank you.

This raised a question by Mr. Clermont. Your method of marketing your debentures and so on is—

Mr. POWELL: This is done through our underwriters and it is sold right across Canada to the general public. It is very widely distributed.

Mr. McLEAN (Charlotte): Mr. Chairman, I would like to ask a supplementary. Is it the intention of RoyNat to issue further preferred stocks—finance through preferred stocks?

Mr. POWELL: I think that is something which will have to be investigated—

Mr. McLEAN (Charlotte): I was just thinking that RoyNat in the minds of the public is backed by the Royal Bank and the Banque Canadienne Nationale. This is fixed in the minds of the public and I think that in their financing through

preferred stock, they would get away with a lower rate by the public thinking that they were backed by the Royal Bank.

Mr. McLAUGHLIN: Mr. McLean, may I answer that? If you issue preferred stock, you have to pay a dividend on it. The reason there is only \$1 million—I think it is \$1 million preferred stock—is a technical one. RoyNat is paying a dividend on that. Once it has paid it for five years it becomes eligible for investment by insurance companies. The \$9 million is left in there in common stock on which no dividend is intended to be paid for some time to build up a larger capital in total so that it can borrow longer from the public. To go to the public now—it is not necessary yet, it still has further borrowing power based on its present capitalization—but to go to the public with preferred stock would mean definitely paying a dividend and would tend to reduce the multiplier—

Mr. McLEAN (*Charlotte*): I meant in the future.

Mr. McLAUGHLIN: That is a question which is hard to answer now because it depends on market conditions as and when RoyNat has borrowed from the public long all that it can based on its present capitalization and retained earnings. It has not reached that stage yet.

The CHAIRMAN: I am sorry. Go ahead, Mr. McLean.

Mr. McLEAN (*Charlotte*): I am talking about the concentration of power. Now, if the eight banks took over RoyNat, would that not be a concentration of power in the eight banks? Would it not be better to have it divided up?

Mr. McLAUGHLIN: I do not know what concentration of power means.

Mr. McLEAN (*Charlotte*): We heard it here at the table—

Mr. GILBERT: I was just repeating what the Porter Commission said.

The CHAIRMAN: Perhaps you gave this information to Mr. Clermont. Do you have any information on who holds these debentures and notes and what segment of the population—

Mr. POWELL: We have them, but they are very widely held by individuals mainly right across the country.

The CHAIRMAN: What about the banks themselves?

Mr. McLAUGHLIN: They do not hold any.

The CHAIRMAN: You have not purchased any?

Mr. McLAUGHLIN: Oh, no. If you are using this as a means of providing long-term lending without tying up your own funds other than the capital it defeats your own purpose if you buy these long-term securities.

The CHAIRMAN: I think that is right. Are there further questions on this specific issue raised by the brief?

(*Translation*)

Mr. Latulippe, do you have questions on the brief?

Mr. LATULIPPE: Yes.

The CHAIRMAN: We are now entering on a general discussion.

Mr. LATULIPPE: I would like to know if RoyNat will lend to school boards and municipalities. Will you buy up debentures issued by school boards?

(English)

Mr. McLAUGHLIN: No, not to municipalities and school commissions: that is not the purpose of RoyNat. The purpose of RoyNat is for industrial loans of the size which are too small for the general market but not the municipalities or school boards.

The CHAIRMAN: I have one thought I want to put to you at this time. I am happy to note the number of offices you have in western Canada—approximately one per province. Why is it in Ontario, which has a much larger population than any of these provinces and quite a large geographical area, you have only one office? The same applies to Quebec, for that matter.

Mr. POWELL: As a matter of fact, we have had to because we have just started to put our staff together. We have concentrated our main operations in the principal cities. Our inquiries come from all points of Ontario into our Toronto office and as soon as they are received there and it gets into an application form our men go out to see the client wherever he may be. We could not afford to open any more branches, that is why.

The CHAIRMAN: I just wondered because, as I say, I am sure we all concur in having offices in the principal cities of the three western provinces; I would not be able to say otherwise. But I was wondering whether or not you might have offices in the other principal cities in Quebec and Ontario. Take Toronto and Windsor, for example—

(Translation)

Mr. LATULIPPE: A supplementary question, Mr. Chairman.

(English)

The CHAIRMAN: Do you have any further information on opening branches in Ontario and Quebec.

Mr. McLAUGHLIN: I do not know what Mr. Powell's plans are for opening other branches but I hark back to what I said before. In a specialized organization like this it is more economical to operate it out of a few offices than it would be for a bank to try to do it out of 1,000 branches. It is concentrated and the men go out when an application comes in.

(Translation)

The CHAIRMAN: Mr. Latulippe?

Mr. LATULIPPE: I would like to know if your interest rates on loans will be based on the CMHC or the Industrial Bank rate. These CMHC loans are at a rate of  $7\frac{1}{4}$  per cent and I believe the Industrial Bank rate is  $8\frac{1}{2}$  per cent.

(English)

Mr. McLAUGHLIN: The national housing rate has no connection with or effect on RoyNat's rate. It does not make residential houses. Its rates are closer to those of the Industrial Development Bank which makes the same type of loans as RoyNat.

The CHAIRMAN: Are we now in a position to begin our general discussion Do you want to begin now, or would you rather recess and begin at this afternoon's session? I declare the meeting recessed. This afternoon Mr. Laflamme will be in the Chair. The meeting is adjourned until 3.45.



## AFTERNOON SITTING

The VICE-CHAIRMAN: Order, please. I will call this meeting to order.

I will ask Mr. Lambert to begin the questioning since he has indicated he has some questions of a general nature on the submission by Mr. McLaughlin.

Mr. LAMBERT: Mr. Chairman, I would like to get the views of Mr. McLaughlin on a number of the features of Bill No. C-222, and if I might run through those very briefly I think we can get on with them.

First of all, I wonder, Mr. McLaughlin, what will be the practical effect from the bank's administrative point of view of the proposal to restrict shareholdings of any one person to ten per cent and also the total foreign holdings to 25 per cent. As a chief administrative officer of the bank can you tell us about some of the problems you might encounter in this regard.

Mr. McLAUGHLIN: I think the easy answer is that I am happy I am the chief administrative officer of the bank and not in charge of the share register. That is going to be an extremely complicated job technically, to follow the transfers.

Fortunately, between Bill No. C-222 and Bill No. C-102 of 1965, a change has been put in where under the present par value of \$10 we do not need to look at under 500 shares. Without that, I do not know how we would have managed it technically. Under 500 shares it is presumed to be Canadian if it is a Canadian address, and is not presumed to be in association with anyone else, unless we have special knowledge of that.

Most of the shareholdings are under 500 shares. It is going to be a difficult job but with time it can be done.

Mr. LAMBERT: Well, do you mean to tell me that because of this lack of necessity to look at anything under 500 shares that it is conceivable that there could be much more than 25 per cent of foreign holdings, if you had a sufficient accumulation of small accounts using a nominal Canadian address but being in essence a foreign holding?

Mr. McLAUGHLIN: I do not think so. If it is a foreign address it is presumed to be foreign. If it is a Canadian address it is presumed to be Canadian. If it is a Canadian nominee, the onus is on the nominee not to vote the shares if they are held actually for a non-resident. So from our checking point of view, it is not impossible.

Mr. LAMBERT: You say the onus is on the nominee holder but if the nominee holder chooses to disregard this injunction not to vote the shares and actually does, and it is done without your knowledge, how do you unscramble the results of his decision to vote those shares?

Mr. McLAUGHLIN: Well, you are asking me on clauses 52 to 57, the most technical clauses in the bill which I must say I have difficulty understanding, but I think you will find the answer in one of the clauses. I do not know whether I can put my finger on it. Mr. Elderkin can probably faster than I can, where what is done at an annual meeting can within nine months be undone if people have voted who should not have voted.

Mr. LAMBERT: But that is an awful way to run the shop, is it not?

Mr. McLAUGHLIN: I did not write the clauses.

Mr. LAMBERT: Well, we will leave those complexities but I must say my own view is that it is going to be easier to honour it in the breach than in the observance.

Mr. McLAUGHLIN: Section 54(5).

Mr. LAMBERT: Well, is it not possibly a better way—the restriction of the ten per cent is the real policeman.

Mr. McLAUGHLIN: That is right.

Mr. LAMBERT: In so far as control is concerned, rather than the 25 per cent.

Then we come to the other matter where the banks are having to unscramble, and that is the question of interlocking directorates or, shall we say, common directorates with certain trust companies or near banks with whom they may enter into competition at the present time or after the act comes into effect. What is going to be the result of either (a) the bank divesting itself of certain directors, or (b) the near banks divesting themselves of the same persons as directors and thereby losing their business knowledge for presumably the reason for which they were appointed to the boards?

Mr. McLAUGHLIN: Well, speaking as a banker and not a near banker, I suggest that the results are going to be more serious for the near banks than the banks, that probably, given a choice two years after the ceiling is lifted, which is the effective date in that particular clause, most of the people who had to give up one or the other would give up a near bank rather than a bank. It is going to cause perhaps a rather severe shortage of directors on the near banks.

Mr. LAMBERT: Well, of course, it is conceivable that one could run for ten years or till the next revision, until clause 18 (6) comes into effect, because if the ceiling does not go off during the lifetime of Bill No. C-222 there is nothing that will affect these directors.

Mr. McLAUGHLIN: That clause will have no effect then.

Mr. LAMBERT: I would like to go to the effects of and have your views on section 75(2)(g) which is popularly known as the Mercantile Bank clause, and ask you what is the extent or the importance in the picture of the operations of your own bank, the operations of your agencies in the United States, and that if retaliatory action is to be taken, I should not say "if", I should say that if retaliatory action is taken what effect will that have on the Canadian banking picture?

Mr. McLAUGHLIN: Do you mean if we were forced to close, say, our New York agency?

Mr. LAMBERT: Well, I suppose it is a bit of a hypothesis as to what retaliatory action might be taken but we know that there is already a bill proposed by one of the American legislators which would have effectively this result, or seriously curtail your operations.

Mr. McLAUGHLIN: Well, any curtailment is very serious. The New York agency is the clearing point for us and I presume for each of the other Canadian banks who has a New York agency, for our overseas business, most of which is conducted in U.S. dollars. I do not mean the U.K. business in sterling and the Brazilian business in its own currency, but the international transactions in foreign exchange are cleared through our New York agency, and, of course, all

our business with the United States, exports and imports. It would hamper us greatly to be restricted in New York.

Mr. LAMBERT: Have you heard of any suggestions of what type of action might be taken in the event that the legislation affecting the Mercantile Bank is deemed to be unduly discriminatory?

Mr. McLAUGHLIN: No, I have not.

Mr. LAMBERT: Is it possible to put a percentage figure on the Royal Bank's operations or the Canadian banking system's operations through the agencies that do exist in the United States?

Mr. McLAUGHLIN: I have not that figure. I do not know that any meaningful figure could be produced that would get the total loans, total deposits of the New York agency that are non-resident. I do not want to confuse two things here. You mention the Mercantile Bank. That is one subject which seems to have risen to the heights of international diplomacy. That is not my feeling. The other is the question of reciprocity and agencies which I think is quite another question.

Mr. LAMBERT: Yes, there is another facet to this, too.

Mr. McLAUGHLIN: Yes, and I think we should, as an international banking system that we have in Canada, give reciprocity and permit agencies on the same basis as we are permitted agencies in the United States. And it is that the agencies of American banks would not be allowed to accept deposits from Canadian residents. They could do some international business. They could make some U.S. dollar loans, but they are doing that in any event without having an agency here. I feel that as a measure of reciprocity that would be the proper step. I think that is an entirely separate question from the Mercantile Bank.

Mr. LAMBERT: Well, they are related to this extent, are they not, though; that they would provide a degree of competition to the Canadian banking system and that those people who favour some control on the ownership of the Mercantile Bank are suggesting that the Mercantile because of its parent organization could come to have a dominant role in the Canadian banking field, and could, shall we say, frustrate monetary policy.

Mr. McLAUGHLIN: It will be some time before it will be that large, I hope.

Mr. LAMBERT: No, but on a realistic basis, I suppose if one asks you are you afraid of the operations of the Mercantile Bank—

Mr. McLAUGHLIN: No, not all.

Mr. LAMBERT: After all, the Mercantile Bank was an entirely foreign-owned bank when it was incorporated, to the knowledge of parliament when it incorporated it, to the knowledge of parliament when the last Bank Act went through. Now, what about the agency side? Would this not provide some competition?

Mr. McLAUGHLIN: It would provide competition but I am not frightened of that, but the alternative might be that we no longer could compete in some other countries.

Mr. LAMBERT: Yes.

Now, if I might turn briefly to another subject, the proposed amendments to section 88 and in particular subsection (5). How do you anticipate that this may affect your business conducted under the aegis of clause 88?



Mr. McLAUGHLIN: Do you mean subclause (5) (b), which is new. There is no change—

Mr. LAMBERT: That is right. The one that encloses a top of \$5,000 on behalf of any unpaid producer.

Mr. McLAUGHLIN: Well, technically we can operate under it, but it will probably mean that for any bank making loans to growers or processors of perishable products of agriculture will have to look far more closely, and it could possibly result in some of the smaller ones without much capital perhaps not being able to get the loans that they would like. It is a possibility, yes.

Mr. LAMBERT: Yes. Well, in other words, it is a question now of balancing which is going to cause the greater harm or which will promote the greater good. I mean promoting the greater good is providing the security to the small producer who in the past sometimes has been hurt when there has been a failure of a processor and the bank had a preferred claim under section 88, or a secured claim under section 88, as against the fact that it is a possibility that in the future there just will not be any financing and, therefore, both the security and the financing have gone and the man might just as well not have engaged in his operations for that year.

Mr. McLAUGHLIN: Well, it will probably be somewhere between that. It is hard to generalize. All I can say is that there will have to be a much closer scrutiny of the credit risks.

Mr. LAMBERT: Fine. The other day I questioned Mr. Paton at some length to see whether we could come up with some definition of the business of banking. I guess you have been aware of that, Mr. McLaughlin. Do you think it is possible to arrive at a definition of banking?

Mr. McLAUGHLIN: Well, so far, no one has succeeded. I think it is extremely difficult to give other than an arbitrary definition. There is one in the Porter Report. You can have as many definitions as there are people attempting to define banking, but I doubt whether it is possible to come up with one that will satisfy everyone, and all purposes.

Mr. LAMBERT: I suppose one might say roughly, that it is those things which we do, viewed from the point of view of the Royal Bank, or from any bank. You readily understand what I am getting at.

Mr. McLAUGHLIN: I do.

Mr. LAMBERT: As I have pointed out, I want to know, for instance, when one crosses a magical threshold under clause 13 of commencing the business of banking, that you cannot commence that business unless you get a certificate from the Governor in Council through the Inspector General. When do you commence the business of banking? This is my point. There are many other instances in this act where banking is defined. I would like to know, for instance, how do you distinguish your operations from those of some of the near banks. In the province of Alberta, how does the Royal Bank distinguish its operations from those of the Treasury Branches? They both get robbed.

Mr. McLAUGHLIN: Yes, but unfortunately when they do it is usually the headline that the bank has been robbed. Maybe that is the definition. To answer that question, in Alberta we derive our powers from the Bank Act, therefore, we

are a bank. I am not a lawyer and I do not know how I could define it other than the simple definition in here.

Mr. LAMBERT: But there is no definition.

Mr. McLAUGHLIN: A bank is a bank chartered under this act. A bank is defined.

Mr. LAMBERT: Yes, it is.

Mr. McLAUGHLIN: A bank means a bank to which this act applies. That is the definition.

Mr. LAMBERT: Mr. McLaughlin, no doubt you would agree that if you explained your operations in that way that you would be out of business in 48 hours.

Mr. McLAUGHLIN: Probably less than that because it does not take very long to explain that one sentence.

Mr. LAMBERT: The Porter Commission came up with some sort of a yardstick of the 100 day obligations, anything less than a 100 day obligations. Do you feel that this might be a useful yardstick to define banking?

Mr. McLAUGHLIN: Not completely.

Mr. LAMBERT: Well, what additions would you make?

Mr. McLAUGHLIN: Well, one of the objections to that is that as I recall, there would be reserves for those institutions which would be banks having deposits of over 101 days, I think it was, but those that were not banks could have deposits of over 101 days without reserves. I submitted a definition to the Porter Commission on Banking but it is an economic definition and has no practical legal—

Mr. LAMBERT: Are you able to summarize it here?

Mr. McLAUGHLIN: In one sentence. A bank is an institution large enough and with the type of customers that it is responsive to open market operations conducted by the central bank. That is a good economic definition of a bank but it is not a practical legal definition.

Mr. LAMBERT: No, that would not catch near banks under any definition.

Mr. McLAUGHLIN: No, and in fact it would not even catch a brand new chartered bank that was so small that it did not have the type of customer and of the size that it was immediately responsive to open market operations. I do not think it is possible to get a legal, I should not say it is not possible, I cannot give you one, a practical operating legal definition of a bank.

Mr. LAMBERT: Thank you, Mr. Chairman.

Mr. GRÉGOIRE: Mr. McLaughlin, would you accept the fact that the operations of the chartered banks described in this pamphlet of the Royal Bank of Canada economic trends and topics from June 1966, that these operations as described in it would constitute the difference between the chartered banks and the near banks?

Mr. McLAUGHLIN: No.

Mr. GRÉGOIRE: Then the near banks could do exactly what is described in here?

Mr. McLAUGHLIN: That pamphlet without a long discussion and repeating a lot that has been said here, talks about a system. We were trying to describe a bank.

Mr. GRÉGOIRE: That is why I am asking you if the operations described here constitute a difference between banks and near banks.

Mr. McLAUGHLIN: No.

Mr. GRÉGOIRE: It does not constitute a difference.

Mr. McLAUGHLIN: That is a description of a system.

Mr. GRÉGOIRE: A system of operation of chartered banks?

Mr. McLAUGHLIN: Well, for that purpose, yes.

Mr. GRÉGOIRE: Can the near banks do what is described here?

Mr. McLAUGHLIN: I want to avoid a long discussion.

Mr. GRÉGOIRE: Of course. Just pick an answer, yes or no. Can the near banks do what is described here?

Mr. McLAUGHLIN: They do not have accounts at the central bank, no.

Mr. GRÉGOIRE: They cannot. Fine.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Chairman, I would like to come back if I may to the first question Mr. Lambert was asking with regard to the agencies. The agencies do operate in New York and other banks operate there. Could you give us some idea of the sort of legislation under which you operate, with the idea in mind at least of possibly introducing legislation of that sort here on a reciprocal basis. I do not know what your legislation is there. How are you restricted?

Mr. McLAUGHLIN: Well, I am afraid I could not summarize the legislation. I do not have it before me but it is simply this, Mr. Cameron, that the agencies of foreign banks receive, subject to annual renewal, a license to do banking business in the state of New York but are prohibited from accepting deposits from American residents. They can make loans, do foreign exchange, and issue letters of credit.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But they cannot accept deposits from Americans, that is the essence.

Mr. McLAUGHLIN: That is the essence.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I do not know really whether you can answer this question. Would you consider that if we made similar reciprocal provisions here, which would be in effect, rather more generous ones because they are bound to apply to the whole country and not to one province or state, that this would constitute a reasonable ground for saying that we are offering reciprocal arrangements?

Mr. McLAUGHLIN: I think it would.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You think it would, and that therefore the suggestion that the removal of the limitations contemplated in this bill on the operations of an American-owned bank would not be required to provide a proper reciprocal arrangement.



Mr. McLAUGHLIN: Well, there are the two things, Mr. Cameron. There is the operation of foreign-owned chartered banks and the operation of foreign agencies. I think the two are quite distinct.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The reason I am linking these together, Mr. McLaughlin, is that they have been linked together in these hearings. In fact, the case that was made against the provisions in this bill regarding the Mercantile Bank was based in the main on the fact that we had to offer reciprocal treatment to an American bank because of the arrangements with regard to agencies of a Canadian bank in the United States. The point I want to get is this. If we established agencies, or the right to establish agencies were granted, that would be sufficient in the way of reciprocity, and we would not have then to consider the question of the treatment of the Mercantile Bank, in this context.

Mr. McLAUGHLIN: Well, do not forget, Mr. Cameron, that we have been discussing this discretion in previous days. I assume this has been largely in relation to the United States. I cannot speak for the United States government, but the Royal Bank of Canada operates in many other countries, and if you do not mind my not revealing the name of the country because we are in rather difficult negotiations right now, we are in trouble in the country where we have operated for perhaps 50 years.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): As an agency?

Mr. McLAUGHLIN: No. In this case, as a branch, because the law would not allow a bank of that country to operate here. I am sure it would never want to. It would not be profitable for it to do so; but I am also reasonably sure that if the law allowed it to have an agency, which it would not want to do, that would be sufficient reciprocity, that we would not have to go through all these delicate negotiations to keep in a country where we have been for fifty years. So it applies to more than just the United States.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Although I think you would admit, would you not, that the concern that has been expressed with regard to the presence of a foreign-owned bank in Canada is much more cogent when that foreign-owned bank is an American bank, in view of the relationship between our two economies?

Mr. McLAUGHLIN: Well, I have not expressed the concern, so I do not know what is in the minds of those who did.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Very good, sir. Would you say, Mr. McLaughlin, that your agency in New York constitutes in any real way competition with the American banking system? I imagine that you exercise the same powers as others do, or you are able to accept deposits from Americans outside the state of New York; is that correct?

Mr. McLAUGHLIN: For non-residents of the United States.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Only non-residents.

Mr. McLAUGHLIN: I believe so. Certainly the state of New York, and I believe it is non-residents of the United States. We can take deposits from anyone domiciled outside that area. I think perhaps we are some competition but not significant. New York is an international money market. To function proper-

ly they must have international banks and I think, probably while the foreign agencies of Canadian and other banks do exercise some measure of competition, the net results to the New York banking system are good, because it makes it even more of an international market.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): They really would not want to get rid of you?

Mr. McLAUGHLIN: I would hope not.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You think it would be unlikely that they would want to get rid of you?

Mr. McLAUGHLIN: Well, I do not think that it would be in their best interests.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Now, to turn to another question, Mr. McLaughlin, there has been before this Committee a number of discussions with regard to the charges made by banks in addition to their interest charges. Perhaps to lay the groundwork for this I should refer you to the hearings of 12 years ago when at that time, as I recall it, only one of the chartered banks was making loans in the personal loan field and charging more than the six per cent; the rest was in service charges. At that time there appeared to be a great conflict of legal opinion, and as I recall it, all the other banks including your own, took this position. As I recall it your predecessor was on the stand, and said that he had legal advice that this was in contravention of the Bank Act. The representatives of the bank that was making these loans said that they had legal advice that it was within the confines of the Bank Act.

Since that time apparently all the banks have decided it is legal. Would it be a fair question to ask you if the system of extra charges which has grown up, leaving on one side altogether the question of whether it is legal or illegal because I am not competent to say, that that increase has to some degree been occasioned and perhaps accelerated by the rise of the near banks?

Mr. McLAUGHLIN: First of all, Mr. Cameron, I think you will find recorded in *Hansard* some years ago a statement of the Minister of Justice that these charges are perfectly legal. To answer the other part of your question, what has brought about the big increase in the consumer loans, because that is what you were referring to, has not been this method of service charge but was what you did ten years ago in changing the Bank Act.

Until 1954, the banks could not take a chattel mortgage. In 1954, they were permitted to take a chattel mortgage from the ultimate consumer and that has brought them, not the extra charge, that was what legally made possible the great increase in the consumer credit.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Do you take chattel mortgages to any great extent?

Mr. McLAUGHLIN: Oh, yes. That is what has made possible these consumers. In other words, in those provinces where it is possible you can take out a chattel mortgage on a car or a T.V. set. Before 1954 you could not. The one bank that was doing that type of business, if you look back at the evidence, and had been for some time, was doing it I believe on two personal endorsements, and not on chattel mortgages. Whether they are still doing it that way or not I do not know,

but that is what opened the door to this big volume at lesser rates than they were paying elsewhere before.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I actually was not confining my question to consumer credit altogether. There has been some discussion also of other demands that have been made by banks. I myself have been informed, and I cannot prove it, I do not know what bank was involved, but I have been informed of people who have made an arrangement with the bank whereby they would pay the statutory interest rate of 6 per cent on say, \$10,000 if they would sign an agreement to pay that 6 per cent on \$11,000 although they were only getting \$10,000 for it. I am told that this has been the case, that there have been these practices developed.

Mr. McLAUGHLIN: You mean that you borrow \$10,000 and pay back \$11,000?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No, no, but you pay interest on \$11,000.

Mr. McLAUGHLIN: Oh, well. I can only speak for my own bank. We do not do that.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You do not do that. There is the question of the standby accounts, or I do not know exactly what phraseology it is, the maintenance of a certain proportion of the loan in the account amounts to really a deduction in the amount that is made available to the borrower, does it not?

Mr. McLAUGHLIN: I am not sure that I know what you mean. If we lend somebody \$100 they get \$100.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Are there not occasions on which customers are asked to keep on deposit a certain proportion of this loan that they have undertaken?

Mr. McLAUGHLIN: Oh.

The VICE-CHAIRMAN: Compensating balances, do you mean?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No, this is another one.

Mr. McLAUGHLIN: Not to my knowledge.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Not to your knowledge. Then the question of compensating balances was brought up once or twice, and there was certain evidence to suggest that the demand for them has been increasing in recent years. Do you know if this is so?

Mr. McLAUGHLIN: Mr. Cameron, you must define what a compensating balance is. With respect to the bank I represent we use that phrase as an alternative, which we give a customer, to an operating charge. If he has a very active account, there is a charge depending upon the balance and the number of entries that go through it. If he does not want to pay a per entry charge, he can carry a larger compensating balance. That is the sense in which we use it. It has been increasing. Our costs are going up. We are analyzing accounts and we are applying operating charges or, since the balance is a factor, if your balance is large enough you may not be charged if there is a compensating balance.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): And this has been increasing?



Mr. McLAUGHLIN: Oh, yes. Yes, as our costs are going up. After all we have been working under a salary floor and a price ceiling.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Could you give us some idea of the ratio between these costs, the ones you mention are overhead costs, of their increase as a ratio of the increase in your volume of business.

Mr. McLAUGHLIN: I am sorry, Mr. Cameron, I brought no statistics with me today. That may be something that the Canadian Bankers' Association could answer. I do not know. All I have with me is Bill No. C-222 and my memory, and it is not very good for figures. I cannot answer that question.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well, one witness we had before us thought there might be some connection between the increase in these arrangements and the rise of the near banks in recent years; in effect, the method of—not evading—but avoiding, shall we say, the 6 per cent ceiling.

Mr. McLAUGHLIN: Well, I think the rise in near banks is partially attributable to the fact that they were able to pay the going rate for money and pass that charge on at a higher than 6 per cent charge.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. McLaughlin, would you consider it likely, or that it could be expected that now, apparently as far as one can judge and as far as the opinions we have had expressed here, with the possibilities of the general level of interests rates into the next several years anyway, that the effective ceiling will be  $7\frac{1}{2}$  per cent when this legislation is passed; that this will be the effect of it? Can we expect that in light of the bank's ability to charge another  $1\frac{1}{2}$  per cent there may be a decline in some of these demands for making charges or for the compensating balances?

Mr. McLAUGHLIN: I do not see that in so far as operating charges are concerned, Mr. Cameron, that there is any connection with the interest rate.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But you will be getting larger returns.

Mr. McLAUGHLIN: If a man or a company is using their account very actively and carrying a very modest balance and that charge goes up or down with the number of cheques that are issued, there is no connection between that and interest rates.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, but I think there is a connection between the return you get on the loans which will be greater at  $7\frac{1}{4}$  per cent than it is at six per cent, and your ability to absorb some of those costs.

Mr. McLAUGHLIN: Yes, but in so far as possible each transaction should stand on its own feet, and a company operating an active account may or may not borrow, and the charge for the operation of the account should be the same whether it borrows or not. If they borrow, then they should pay whatever the competitive going rate is for the loans, but that should not affect the operation of their account. They are two separate things.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Now, I had one other question I was asked to put to you. I do not know whether it is one of your customers but a customer of one of the banks. The question is this. Why is it that

the banks pay interest on the minimum balance rather than on the average balance over the three months period, I think it is?

Mr. McLAUGHLIN: Because we do not have the average balance to use.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well, how do you get the minimum? How do you establish the minimum?

Mr. McLAUGHLIN: Well, it is the lowest balance.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But you have also got the highest balance, have you not at the end of the period?

Mr. McLAUGHLIN: Mr. Cameron, if you have \$100 in the savings account and for one day during the month had \$100,000 in it, that gives you a pretty high average for the month, but we only have that \$100,000 for the one day. You cannot pay interest that way.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But is the reverse not also true; that a customer may have for every day in the period, except one, a substantial balance and owing to his necessity for making some payment for which he is going to make a deposit the next day, he reduces it for that one day, and he gets only interest on that.

Mr. McLAUGHLIN: Yes; there are dozens of ways of calculating interest but that is taken into consideration when the rate is set. If you were to pay on the average during the month you would get a much lower rate. You would have to. It is a question of arithmetic.

The VICE-CHAIRMAN: You have some other questions. Mr. Cameron?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You might. I do not find your answers too convincing, Mr. McLaughlin. I will have to think about it.

The VICE-CHAIRMAN: Thank you, Mr. Cameron.

(Translation)

Mr. Clermont, please.

Mr. CLERMONT: Mr. McLaughlin, do you know of any Canadian chartered bank which operates in the States on the same basis as Canadian banks in Canada, which receives deposits from the American public?

(English)

Mr. McLAUGHLIN: If I understood your question correctly, Mr. Clermont, there are a number of—at least two Canadian banks—which have wholly owned subsidiaries chartered in various states of the United States.

(Translation)

Mr. CLERMONT: Are they part of the Federal reserve of the United States? Do they have a federal permit or only a state one?

(English)

Mr. McLAUGHLIN: I do not know the answer to that. The Royal Bank of Canada is not in that situation. There are two banks which are but I cannot answer whether they are state banks or national banks. I suspect they are state banks.

(Translation)

Mr. CLERMONT: In other words, you do not know if there is a Canadian bank which operates in the United States enjoying the same privileges as the Mercantile Bank in Canada?

(English)

Mr. McLAUGHLIN: Oh, yes, there are two. The Bank of Montreal has a subsidiary or subsidiaries.

Mr. CLERMONT: That is not what we were told last week.

The VICE-CHAIRMAN: No, but he said that there were state banks.

Mr. McLAUGHLIN: And Canadian-Imperial has the same thing.

Mr. CLERMONT: I know about the Canadian-Imperial Bank but we were told last week, I think by Mr. Hart, that their branch in New York is an agency.

Mr. McLAUGHLIN: Oh, this is in New York?

Mr. CLERMONT: California.

Mr. McLAUGHLIN: California. Well, I think it is a separate incorporation, although I am not knowledgeable about the details.

(Translation)

The VICE-CHAIRMAN: Are you through?

Mr. CLERMONT: Yes.

(English)

Mr. LEBOE: Mr. Chairman, I have a very, very simple question. Mr. McLaughlin may prefer to have me wait until we get trust companies before us, but since his bank is involved with trust companies, I am wondering whether Mr. McLaughlin could tell the Committee if the trust companies create deposits by virtue of making a loan.

Mr. McLAUGHLIN: I would refer you to the Porter report which I think answers that very succinctly in one sentence. I have not mine with me.

Mr. LEBOE: I have not either. Do you remember what it is?

Mr. McLAUGHLIN: The answer is yes.

Mr. LEBOE: That is the answer I was looking for. Thank you, Mr. Chairman.

Mr. WAHN: Returning to a question asked earlier about the \$5,000 preference for producers over the section 88 security of the bank, I believe you said, Mr. McLaughlin, that it is possible that in certain cases this might make it more difficult for the bank to extend a loan to a processor.

Mr. McLAUGHLIN: We would have to assess the risk very carefully.

Mr. WAHN: I presume that most processors would be corporations.

Mr. McLAUGHLIN: I think they are.

Mr. WAHN: It was my understanding that the banks on occasion at any rate take debentures or securities of that type from corporations to secure a line of credit. Does your bank do that on occasions,

Mr. McLAUGHLIN: Are you talking about processors, or in general?



Mr. WAHN: Well, in general, any business man, any corporation who wants to make a loan.

Mr. McLAUGHLIN: On occasion, yes.

Mr. WAHN: And you could do this in the case of a processor as well.

Mr. McLAUGHLIN: You would get security, if it was not otherwise pledged, on the equipment in the plant. I do not know whether you could get it on the green peas that came in today and went out in cans tomorrow. I am not a lawyer; I do not know whether you can cover it that fast.

Mr. WAHN: A debenture ordinarily contains a general floating charge, as you probably realize, as well as sometimes a specific mortgage. If this were so, unless something were put in the Bankruptcy Act to the same effect as the provision in the Bank Act, in effect, the protection which was intended to be accorded to the producer could be circumvented by the bank taking a debenture, could it not?

Mr. McLAUGHLIN: I am afraid I am not a lawyer and I do not feel qualified to answer that technical question.

Mr. WAHN: Well, your bank does take debentures though to secure a continuing line of credit.

Mr. McLAUGHLIN: On occasion, yes.

Mr. WAHN: What quarterly period is used by your bank in computing the interest rate.

Mr. McLAUGHLIN: The same as them all. The year starts on the first of November; October 31st is the year end and you run your quarters from November 1st.

Mr. WAHN: Do you know whether information as to the quarterly period is given in your safety deposit books which you issue to your customers?

Mr. McLAUGHLIN: I have not seen one for so long I do not know.

Mr. WAHN: Do you know whether in any of your banks there is any notice notifying your customers of what the minimum quarterly period is? Have you seen one?

Mr. McLAUGHLIN: Well, it may be in the small print in the front of the Pass Book along with the term of notice of withdrawal. I do not even know that that is.

Mr. WAHN: My next question is what method do you adopt of making known to your customers this limitation on their right to interest?

Mr. McLAUGHLIN: Well, they are told when they open an account. You mean what the rate is and the method of calculating it?

Mr. WAHN: Yes.

Mr. McLAUGHLIN: I think it is such a common matter that it is almost common knowledge; Three per cent of the minimum quarterly balance.

Mr. WAHN: Do you think that many people know about the minimum quarterly balance provision?

Mr. McLAUGHLIN: Oh, I think so.

Mr. WAHN: And what the quarter is?

Mr. McLAUGHLIN: Oh yes. After all they know when the interest is credited.

Mr. WAHN: When is the interest credited?

Mr. McLAUGHLIN: Twice a year.

Mr. WAHN: On what day?

Mr. McLAUGHLIN: October 31, and six months thereafter.

Mr. WAHN: On October 31 you would credit interest in respect of what period?

Mr. McLAUGHLIN: Six months prior.

Mr. WAHN: For the six months period ending when?

Mr. McLAUGHLIN: Ending October 31.

Mr. WAHN: You credit it on that day. You must make the computation on the very date you credit it?

Mr. McLAUGHLIN: Well, from a technical point of view it is often made up until a day or so before, then at the end of the year there is a great deal of work doing it at the last minute.

Mr. WAHN: The Porter Commission, I think Mr. McLaughlin, emphasized the importance of competition within the banking system in Canada and witnesses who have appeared before this Committee have emphasized desirability of this as well. In general terms, would you be in favour of more competition within the banking industry in Canada?

Mr. McLAUGHLIN: I do not see how there could be any more, other than more banks.

Mr. WAHN: You mean the Porter Commission was incorrect in saying that there was not sufficient competition within the banking industry in Canada?

Mr. McLAUGHLIN: Well, as a banker who is on the firing line every day, I can tell you the competition between the banks is extremely keen.

Mr. WAHN: I think it is almost an article of faith so far, as indicated in the Porter Commission, there should be more competition within the—for example, more competition between the banks and near banks. The banks are given a greater opportunity to compete with the better financial institutions and other financial institutions should be given more opportunities to compete with the banks. Now this is a very clear feeling that I have had. Am I incorrect in that?

Mr. McLAUGHLIN: I have no objection to that if we can go into other fields or other institutions are permitted to go into our fields provided the rules of the game are the same.

Mr. WAHN: This would involve an increase in competition.

Mr. McLAUGHLIN: That is right.

Mr. WAHN: I put my question again. In general terms are you in favour of more competition in this field in Canada or not?

Mr. McLAUGHLIN: I think what you are trying to say is are there more institutions competing for the same dollar. That is perhaps another way of more competition.

Mr. WAHN: That is not what I intended to say.

Mr. McLAUGHLIN: I think that is the result. I have no objection.

Mr. WAHN: I intended to ask whether you were in favour of more competition.

Mr. McLAUGHLIN: I have no objection to it whatsoever.

Mr. WAHN: But are you in favour of it? I hate to be so persistent but it is a very simple question.

Mr. McLAUGHLIN: I do not think it is ever asked of a businessman to volunteer that he wanted more competition, but if it happens, it happens. I do not object to it.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): There is no good objecting to it.

Mr. McLAUGHLIN: There is no good objecting to it but I am not going to ask for it. It is bad enough as it is now.

Mr. WAHN: Are you in favour of the bank being permitted to compete more freely with other financial institutions?

Mr. McLAUGHLIN: Well, Bill No. C-222 permits us to do that in mortgages and to the extent that we can compete in anything more. I am all in favour of it.

Mr. WAHN: It has also been suggested that perhaps the near banks should be given a greater opportunity to compete with the banks. Are you in favour of that?

Mr. McLAUGHLIN: Provided they do so under the same rules, I have no objection whatsoever.

Mr. WAHN: I do not want to put words in your mouth but I would have thought you are in favour of greater competition generally among the financial institutions in Canada, on the basis of what you have said.

Mr. McLAUGHLIN: Well, we have come back full circle; I cannot object to it but one would not ask for it.

Mr. WAHN: Well, would more competition in the banking field in Canada tend to develop a more effective, perhaps a more international money market in Canada.

Mr. McLAUGHLIN: No; I do not think so. Canada is a world trader but the Canadian dollar is not an international currency. Most of the transactions, both in imports and exports, are done on the basis of sterling or U.S. dollars. I do not think that ten more banks would make any difference to that.

Mr. WAHN: Some have suggested that if foreign banks were permitted to compete more freely in Canada they could provide additional services and tend to develop a more effective and more efficient money market. Would you agree?

Mr. McLAUGHLIN: I do not know of a service that foreign banks can provide that is not already being provided by the existing chartered banks.

Mr. WAHN: So that you feel it would serve no useful purpose to let foreign banks engage in banking activities in Canada.

Mr. McLAUGHLIN: I did not say it would promote no useful service. It would increase competition, but I do not think it would add any new service.



Mr. WAHN: Would that competition be in the interests of the Canadian public, in your view?

Mr. McLAUGHLIN: Well, we are back to competition again. I suppose any competition is in the interests of the public.

Mr. WAHN: So that permitting foreign banks to compete in Canada would in your view create more competition and it might possibly at any rate inure to the benefit of the Canadian public.

Mr. McLAUGHLIN: I do not think it would harm them. I do not know whether it would do them any good. It is not as if there was nobody competing now. If you add one or two more—

Mr. WAHN: I do not know whether this next question has been asked. If it has, I apologize, Mr. Chairman.

Mr. McLaughlin, would you be in favour of permitting foreign banks to operate in Canada through subsidiaries?

Mr. McLAUGHLIN: Through agencies.

Mr. WAHN: Well, first through subsidiaries.

Mr. McLAUGHLIN: Do you mean through a chartered bank?

Mr. WAHN: Yes.

Mr. McLAUGHLIN: No, I think that our chartered banks as such should be Canadian owned.

Mr. WAHN: Right. Then would you be in favour of permitting foreign banks to act through their own branches?

Mr. McLAUGHLIN: Well, I would through agencies. I do not know quite what you mean by through a branch. I do not know how a foreign bank can operate a branch in Canada under this.

Mr. WAHN: What I had in mind was just that you have corporations carrying on businesses in Canada through branches which are licensed to do business.

Mr. McLAUGHLIN: Well, that is not applicable under the Bank Act. It would be I think an agency or a chartered bank.

Mr. WAHN: Yes.

Mr. McLAUGHLIN: For agencies I have no objection. I would welcome them.

Mr. WAHN: Your objection to a branch, if it were permitted, would be the same as to the subsidiary, presumably.

Mr. McLAUGHLIN: I suppose there is not much difference between a branch and an agency. My objection would be, I think—an agency not being permitted to take deposits from Canadian residents is going to engage largely in foreign business, therefore, it is not going to be a major factor in banking in Canada. It will be in the international field and make some U.S. dollar loans. I do not know how to answer your question with respect to branches because I just do not see how they fit into our system.

Mr. WAHN: Yes, I can see that. With the general shortage of capital in Canada and indeed throughout the world it would be desirable for Canada to

attract as much floating transient capital as possible. Have you or your bank ever given any thought to possible methods of attracting this transient capital to Canada along the lines perhaps that this has been adopted by the Swiss banking system?

Mr. McLAUGHLIN: Floating capital which we can attract is only useful to us in Canada if it is Canadian dollars.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): If it does not float too quickly.

Mr. McLAUGHLIN: But one cannot use sterling or French francs in Canada. If it is floating and you catch it, you use it in the area in which sterling or French francs or Deutsche marks are usable. It does not help the Canadian situation unless it is converted and if it is floating it is probably not for permanent conversion.

Mr. WAHN: Why would it not be converted if the Canadian dollar is reasonably stable? Take deposits for example from French residents, if you attracted deposits from French residents or German residents or European residents generally, why would it not be convertible?

Mr. McLAUGHLIN: Well, first of all we are using bad examples. I do not think those French francs or Deutsche marks are probably available under their exchange regulations but, if they were, it is not much use to attract a million French francs for 30 days, go through the expense of a swap and have to convert to French francs at the end of 30 days. It is not much use in Canada. We want more permanent investment.

Mr. WAHN: If you receive deposits from non-residents, do they not serve the same purpose as any other deposit as far as the extension of credit is concerned?

Mr. McLAUGHLIN: It is not the residency of the deposit that counts; it is the country. And if we receive Canadian dollars from a French resident or a German resident, that is fine. But Deutsche marks are only usable in Germany.

Mr. WAHN: Well, I think many of us have the impression that the Swiss have done quite well by the development and elaboration of their banking system. I have no personal knowledge of its details except that I understand they do maintain secrecy of non-resident accounts, for example, and it does tend to attract capital to the country even if it is transient. I have always had a feeling that if enough money is floating around that sometimes gold dust clings to the fingers of those through whom the money passes, and if enough of it was in Canada some of it might remain here.

Mr. McLAUGHLIN: If we could make Canada an international money market, it might, but the facts of life are that the Canadian dollar is not an international currency on the scale of the U.S. dollar, sterling or the Deutsche mark.

Mr. WAHN: What about the Swiss?

Mr. McLAUGHLIN: Well, the Swiss deal mainly in foreign currency.

Mr. WAHN: Well, really my question is, has any study been made of a system, such as the Swiss system, to see if there are any advantages which it has which should be introduced into the Canadian banking system?

Mr. McLAUGHLIN: The subject of the numbered bank accounts?

Mr. WAHN: Well, that among other things.

Mr. McLAUGHLIN: No. I do not know of any; not to my knowledge.

Mr. WAHN: I am not just speaking of the numbered bank accounts which Mr. Cameron seems to find so amusing. I am not as familiar with that particular aspect as he apparently is but the Swiss banking system generally is considered a fairly sound sensible banking business. Am I right?

Mr. McLAUGHLIN: Well, I think so.

Mr. WAHN: Is it not conceivable that some characteristics of that system might serve as a useful precedent to Canadian bankers or have we focused all—

Mr. McLAUGHLIN: I do not know of any. I think the situations are so dissimilar—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Chairman, may I ask a supplementary question. Does the location of the Bank of International Settlement at Basle in Switzerland not have some bearing in their operations in foreign currency?

Mr. McLAUGHLIN: I would think it would.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It gives them a preferred position in that regard.

Mr. WAHN: Mr. McLaughlin, am I to believe that to your knowledge no bank nor any organization of banks has made a study of other leading banking systems throughout the world, and I am speaking particularly of the Swiss system, to see whether there could conceivably be some features that could with advantage be introduced into the Canadian system?

Mr. McLAUGHLIN: We have from time to time looked I guess at the banking laws of most countries and if we find anything that would be advantageous in Canada it is usually discussed before each revision, and I cannot think of anything that has been incorporated into this from the Swiss system.

Mr. WAHN: Well, specifically, you do not feel that there is anything in the Swiss system which could be introduced to advantage.

Mr. McLAUGHLIN: Not to my knowledge.

Mr. WAHN: Thank you, Mr. Chairman.

The VICE-CHAIRMAN: Thank you, Mr. Wahn. Mr. Grégoire.

(Translation)

Mr. GRÉGOIRE: Mr. McLaughlin, to come back to your newsletter, I received a copy from you on the 8th of September, 1966 when I wrote to ask you for your comments on this publication and you wrote to me "It is clearly understood that I am entirely in agreement with the text" and it was signed Mr. McLaughlin, Chairman and President. You said, "It is clearly understood that I am fully in agreement with the text". In the text, Mr. McLaughlin, in pages 4 and 5, I find and I quote:

(English)

"Banks Acquire Additional Loans and Securities of \$92 million  
Causing their Deposits to Increase by \$92 million"



(Translation)

when they have \$8 million in cash reserve. You are in agreement with this operation that the chartered banks are conducting as described herein?

(English)

Mr. McLAUGHLIN: I do not disagree with anything that is said in that pamphlet.

(Translation)

Mr. GRÉGOIRE: If you are in agreement with this banking operation conducted by the chartered banks, you admit that the loans by chartered banks precede deposits made in them?

(English)

Mr. McLAUGHLIN: I would refer you to the monthly or annual statement of a bank where you will find that the deposits exceed the loans.

(Translation)

Mr. GRÉGOIRE: In the process of expansion of credit in Canada, do you agree that loans come before deposits, and it is precisely because loans take precedence over deposits that there is an expansion in credit?

(English)

Mr. McLAUGHLIN: Well, Mr. Grégoire, I do not want to get into a long involved discussion which is a repetition of what has happened before. When you ask, do loans come before deposits, that is the translation I received, I do not know whether you mean does the chicken come before the egg, but deposits always are greater than loans.

(Translation)

Mr. GRÉGOIRE: That is not what I am asking you. I only want to know whether the expansion in credit is due precisely to the fact that loans take precedence over deposits as specified here in the newsletter where it states that when the system of chartered banks generally increase their reserves by \$8 million, they acquire additional loans and securities "causing their Deposits to Increase by \$92 million".

(English)

"Banks acquire additional loans and securities of \$92 million causing their deposits to increase by \$92 million."

Mr. McLAUGHLIN: But the translation may not be correct. You asked, do loans take precedence over deposits. If that translation is correct deposits always take precedence over loans.

Mr. GRÉGOIRE: Would you repeat that, please.

Mr. McLAUGHLIN: The translation came through that you asked me did loans take precedence over deposits.

Mr. GRÉGOIRE: No, no.

Mr. McLAUGHLIN: That is the way it came through.

Mr. GRÉGOIRE: No, I did not.

(Translation)

I asked whether, in the expansion of credit for all the chartered banks, as is mentioned here that when all the chartered banks acquire surplus of \$8 million in their reserves, it states and I quote:

(English)

"Banks Acquire Additional Loans and Securities of \$92 million Causing their Deposits to Increase by \$92 million".

(Translation)

In view of this, do you think that in the expansion of credit the loans come before the loans in the process of expansion of credit?

(English)

Mr. McLAUGHLIN: No. It is a simultaneous interest.

Mr. LEBOE: I wonder if I could ask a supplementary question. Is it not true, Mr. McLaughlin, that when a man has a note accepted by the bank, it becomes immediately an asset of the bank once it is accepted and signed by the individual.

Mr. McLAUGHLIN: That is correct.

Mr. LEBOE: The next step then is the placing of the credit figures to the credit of the account of the individual, creating a deposit.

Mr. McLAUGHLIN: Sometimes.

Mr. LEBOE: Mostly.

Mr. McLAUGHLIN: He may want to walk away with the cash.

Mr. LEBOE: Yes, but—

Mr. McLAUGHLIN: That often happens.

Mr. LEBOE: But most the time when that happens they have a gun in their hand. But the normal banking procedure is that a man creates a deposit—

Mr. McLAUGHLIN: Either in that bank or some other.

Mr. LEBOE: Eventually, yes, but in the system it will all come out in the wash anyway. Is it true then that this becomes a deposit and your statement that the deposits always exceed the loans takes into account that the loan becomes a deposit and in addition you have the savings deposit in addition to the deposits which are created as a matter of a loan being taken out. Is that right?

Mr. McLAUGHLIN: No. When a man borrows he can take cash; he can deposit the proceeds of the loan either in a current account or a savings account. There is no segregation.

Mr. LEBOE: I realize that but I am talking about the normal practice. If a man takes out a loan personally, I think he would be awfully stupid to take out a loan at a bank at 6 per cent and put it into a savings account. I think this would be rather stupid. I do not think he would do this, would he, not normally?

Mr. McLAUGHLIN: No; it is. Because unfortunately savings accounts are subject to cheque, and he may put it in there and if he does not take the cash he may write a cheque right away and the deposit is not there tomorrow. That is only a matter of convenience.

Mr. LEBOE: Yes, but these are relatively small things, insignificant amounts of money compared to what the bank does in its business, I mean; otherwise, we would have a lot more currency operating our business than what—

Mr. McLAUGHLIN: We pay by cheque.

Mr. LEBOE: What are the currency operations, about 4 per cent of the total volume of business?

Mr. McLAUGHLIN: I do not think you measure what—

Mr. LEBOE: I think it is around 4 per cent.

Mr. McLAUGHLIN: I do not know how you measure, whether you buy a package of cigarettes by cheque or by cash. I do not know how you measure the cash part of it. You can count the cheques but—

Mr. LEBOE: It is generally conceded it is around about that, but I would like to hold you to the principle rather than getting off on the little side issues and getting off the beaten track here. The deposit that was created by the loan normally if deposited is a credit to the individual borrower, right?

Mr. McLAUGHLIN: Temporarily until he writes a cheque against it.

Mr. LEBOE: Well, I am interested in the mechanics, I am not interested in what he does afterwards because this has a direct bearing on the question that is being asked by Mr. Grégoire, and what he is trying to get out of you as a witness, because you made the statement twice or three times that the deposits exceed the loans. But it must take into account the deposit that is created by a loan.

Mr. McLAUGHLIN: That is right.

Mr. LEBOE: This is the question that undoubtedly Mr. Grégoire is trying to get you to put in simple language, and I think that if we were to stay away from getting into the little technicalities such as the individual writing cheques on it because surely in the banking system it does not disappear. It does not disappear because what is one man's grief is another man's happiness in this kind of thing. If the other fellow does the same in the other bank, with the exception surely of the near banks, and this brings me to another question, related if you do not mind, and that is, would not the system of the bank themselves rather have compensating balances than to pay services charges, and would they not rather have a compensating balance in their account.

Mr. McLAUGHLIN: The choice is the customer's.

The VICE-CHAIRMAN: I am sorry to interfere, Mr. Leboe, you asked to put a supplementary question but I can hardly call your question that now. It may be supplementary, but—

Mr. LEBOE: I think it is directly related to the question that was asked by Mr. Grégoire. I think it ties right in.



The VICE-CHAIRMAN: Yes, but Mr. Grégoire had the floor and unless he gives you permission to ask more questions I think you should be fair and ask them later.

Mr. LEBOE: I am in your hands. I just thought that to follow the thing through—

The VICE-CHAIRMAN: Unless you are both in the same line—

Mr. GRÉGOIRE: They are directly related to mine. I yield the floor.

Mr. LEBOE: Yes, it is directly related to the question that Mr. Grégoire has asked.

The VICE-CHAIRMAN: All right. Go ahead.

Mr. LEBOE: This is not a question of whether or not it is the choice of the depositor. Is it not a fact that compensating balances are more valuable to the banks or the banker, whichever the case maybe, than collecting a few pennies, shall we say, for servicing accounts?

Mr. McLAUGHLIN: I would say it is probably six of one and half a dozen of the other. If you have larger deposits you will be able to earn something. If you do not have the deposits you get some income from the service charge. It ends up the same in both cases.

Mr. LEBOE: You think it is about a fifty-fifty proposition. Thank you.

Mr. GRÉGOIRE: If I may take a few moments at this point, on page 6 you have two sentences I would like to read to you, Mr. McLaughlin, because it is written by the Royal Bank of Canada and I think it is the best document ever written by a chartered bank.

Mr. McLAUGHLIN: Mr. Grégoire, do you agree with it?

Mr. GRÉGOIRE: Completely. I completely agree with all this, except that what is done here by the chartered banks, I would like to see done by the Bank of Canada. That is the difference.

On page 6, the first paragraph, do you want a copy?

Mr. McLAUGHLIN: No, I have a copy.

Mr. GRÉGOIRE: It is written:

Cash is a non-earning asset and excess cash means an unnecessary sacrifice of earning power.

The second sentence is:

The banks will therefore use up any excess cash immediately by making loans or buying securities, thereby restoring the original level of deposits

Is that what we can call the operation of expansion of credit?

Mr. McLAUGHLIN: Part of the central bank's open market operations, I would say.

Mr. GRÉGOIRE: Yes, if the central bank, for example, put in circulation \$8 million more which goes back to chartered banks as a reserve then they will use

this excess cash immediately by making loans or buying securities, thereby restoring the original level of deposits. Is that what you call the expansion of credit, the operation of the expansion of credit?

Mr. McLAUGHLIN: I imagine that is what you would call it.

Mr. GRÉGOIRE: Then they will use that excess cash by making loans or buying securities. That is the first operation of the expansion of credit, and the second operation of the expansion of credit is described here thereby restoring the original level of deposits. Is that a fact?

Mr. McLAUGHLIN: That is what it says.

Mr. GRÉGOIRE: Yes. So you agree with that. Then when they have the excess cash first, make loans; that is a part of expansion of credit. They make loans because they have excess cash, and the second part of this operation of credit will be the deposit that will follow loans immediately.

Mr. McLAUGHLIN: Or buying securities.

Mr. GRÉGOIRE: I mean loans or buying securities.

Mr. McLAUGHLIN: Well, you must be very careful. You cannot force people to borrow.

Mr. GRÉGOIRE: Do you have difficulty finding borrowers, or do you refuse some?

Mr. McLAUGHLIN: I am talking in general terms. There are times.

Mr. GRÉGOIRE: Which one do you have more difficulty to find borrowers or depositors?

Mr. McLAUGHLIN: Depositors, sir.

Mr. GRÉGOIRE: Then you do not have any difficulty finding borrowers?

Mr. McLAUGHLIN: At the moment there is quite a demand.

Mr. GRÉGOIRE: I think that has been clarified. I asked that question because when Mr. McIntosh comes back, it will be clarification for him.

Mr. McLAUGHLIN: That is right.

Mr. GRÉGOIRE: You said in answer I think to Mr. Wahn that Canadian banks as such should be Canadian owned. I wrote down that sentence.

Mr. McLAUGHLIN: I do not know if those were my exact words but it is my sentiment.

Mr. GRÉGOIRE: Yes, Canadian banks as such should be Canadian owned.

*(Translation)*

I want to put you a question in regard to this. In the event that Quebec should achieve independence by a free and democratic decision by vote, would you as Chairman of the Royal Bank of Canada, whose head office is in Montreal, one of the biggest banks in Canada, do you think that Canada and Quebec, then becoming two different countries, would the Royal Bank then have two head offices, and two distinct administrations, one in Canada and one in Quebec. I want to complete my question, would the Royal Bank of Canada be

ready to co-operate when that event would occur, and I repeat, through the free and democratic choice of the Quebec voters?

(English)

Mr. McLAUGHLIN: Well, Mr. Grégoire, that is a pretty hypothetical question, and I have not given any more thought to where our head office might be under those circumstances than I have to where it might be if Canada took over the United States.

(Translation)

Mr. GRÉGOIRE: In other words, Mr. McLaughlin, you do not want to answer the question as asked?

(English)

Mr. McLAUGHLIN: It is a hypothetical question I cannot answer.

(Translation)

The VICE-CHAIRMAN: Do you have any more questions, Mr. Grégoire?

Mr. GRÉGOIRE: Mr. Chairman, if Mr. McLaughlin allows me to make a remark, no, rather the Bank Act is amended every ten years. My question might be hypothetical, but perhaps in ten years it will not be any longer. This is why after the declaration I made that "Canadian banks as such should be Canadian-owned", if Quebec becomes independent, do you believe that banks in Quebec should be Quebec-owned? I wonder whether the Royal Bank would be prepared to collaborate with these banks?

(English)

Mr. McLAUGHLIN: Mr. Grégoire, you are still in the realm of hypothesis. I cannot answer the question.

Mr. GRÉGOIRE: Would you repeat that, please?

Mr. McLAUGHLIN: You are still in the realm of hypothesis. I cannot answer the question.

Mr. FLEMMING: Mr. McLaughlin, a few minutes ago I think in reply to a question from Mr. Lambert you mentioned your concern if there was any legislative action in the United States either federally or by state legislatures in connection with any action that might hamper the operations of your agency in that country.

Mr. McLAUGHLIN: I would be concerned, yes.

Mr. FLEMMING: My question is then, would your concern be entirely from the point of view of the well being of your institution, or would it be partly the well-being of this nation?

Mr. McLAUGHLIN: Oh, certainly, both.

Mr. FLEMMING: Would you like to elaborate?

Mr. McLAUGHLIN: Well, as the President of the Royal Bank of Canada I would hate to see any step taken which might reduce its size and its earning power. That is the answer to one side.



The answer to the other is: If, perchance, and again this is rather hypothetical, the Canadian banks are not permitted to have agencies in New York then we would be, as a nation, dependent on others to do a lot of the financing of our foreign trade and foreign exchange. I would hate to see that.

Mr. GRÉGOIRE: Mr. McLaughlin, why is it that you answer a hypothetical question once and not before?

Mr. McLAUGHLIN: Yours was the second degree of hypothesis.

Mr. FLEMMING: I do not think that, with great respect to Mr. Grégoire, the same thing applies because we have by press reports a suggestion that we may be liable for legislative action in connection with the attitude that has been taken in connection with the Mercantile Bank. It is in the newspapers. It is no secret, is it?

Mr. McLAUGHLIN: No. Well, I have read it in the newspapers but what has actually happened to date is not to take it.

Mr. FLEMMING: That is what I was saying, nothing has happened.

Mr. McLAUGHLIN: Nothing has happened.

Mr. FLEMMING: But we are concerned and I have a special interest in connection with United States trade. It is as a citizen and as an exporter also. It seems to me that we as a committee studying banking operations and making a ten year correction, if you like, and I think that is what we think, an improvement; I am sure that it is our aim and objective, and your aim and objective in appearing here today is to contribute toward an improvement in the Bank Act which will be the governing feature of all the operations for the next ten years, that being so, it seems to me that we have to take notice of any action that may be contemplated that will interfere with our trade with our best customer. Is that correct?

Mr. McLAUGHLIN: Correct.

Mr. FLEMMING: I am trying hard to get you to disagree, Mr. McLaughlin, but I am not making very much headway.

I will go into another subject. I seem to recall your expressing some very forthright opinions in connection with—this may not be recently but at one time—the whole question of tight money. I just wonder if with respect to the present tight money situation which everyone who has appeared here, and I am sure every member of the Committee, faces—and I am sure we have all faced it in our day to day conversations and correspondence with our constituents—you have any views on what might be done that is not being done that might have a tendency to correct it.

Mr. McLAUGHLIN: You are implying that it should be corrected. If that is the case—

Mr. FLEMMING: I am implying that there are parts of the country where the tight money situation is imposing real hardship.

Mr. McLAUGHLIN: I think the Governor gave an excellent answer when he appeared here. I would like to say this, Mr. Flemming, that as difficult as it is to operate under, I do not disagree with the present over-all tight money policy.

One can always argue, in fact argue endlessly, whether it should have been just a little tighter or a little less tight. On the whole, I think the Governor of the Bank of Canada has done a most commendable job.

It is true, as he said, that tight money is impersonal and sometimes it may hit some people or some areas a little harder than others. Certainly, in so far as the bank I represent is concerned, we do our best to take this into consideration.

Mr. FLEMMING: Do you think that a curtailment of credit is any more effective in dealing with a situation of tight money than would an increase in the amount of goods? In other words, the old saying is, that inflation is too much money chasing too few goods. Do you deal with that situation any better by curtailing credit than you would by increasing the supply of goods?

Mr. McLAUGHLIN: I think both steps are necessary. You should always do all you can to increase the supply of goods if the demand exceeds them but until that happens if you increase the money supply too rapidly you get quite rapid inflation.

Mr. FLEMMING: Do you think that at the present time with the day to day knowledge that you have the inflation situation has improved in the last few months under the tight money regulations, if you like?

Mr. McLAUGHLIN: Well, tight money is only one of the steps that should be and has been taken. I still think there is some threat of inflation around the country. I would not want to see today the money supply increased drastically. I think it would lead to rapidly rising prices.

Mr. MONTEITH: Mr. Chairman, may I interject here. In what way would it contribute to a rapid increase in prices? What would the mechanics of this be?

Mr. McLAUGHLIN: Well, that is a long, complicated answer, I would think. I will be very brief.

At the present time the banking system is unable to meet the total demand for loans. Let us assume that the money supply overnight is increased sufficiently by the central bank so that once more we got back to what some bankers call the good old days when, having assessed the credit risk, that was the end of it, you made the loan. And let us assume that somebody wanted a loan to build an apartment. That is not the end of the story because if he cannot get the men and material—they are still in short supply—all he does is bid for them to get them from somebody else. There are no more men and there is no more material, and he will be outbid.

Mr. MONTEITH: What if the loans were made to manufacturers to provide the materials?

Mr. McLAUGHLIN: Well, there you are getting into—let me ask you one more question before I answer it. Who would make that decision?

An hon. MEMBER: That is why we need economic planning.

Mr. MONTEITH: I think economic planning is about the same stage today as medicine was in the days of Louis XIV.

An hon. MEMBER: Unfortunately.

The CHAIRMAN: Order. Order, please.

Mr. FLEMMING: We will stay with general subjects, Mr. Monteith. I assume, Mr. McLaughlin, that in your assessment of an application you do take into consideration whether the purpose for which the loan is requested is for general productivity or otherwise.

Mr. McLAUGHLIN: Oh, yes we do.

Mr. FLEMMING: And if it qualifies under that heading, then I assume that you look on it with a good deal more favour than if it were something that was not going to contribute to the general productivity of the country.

Mr. McLAUGHLIN: It has a high priority under those circumstances.

Mr. FLEMMING: I think my final question at the moment might be along this line. In your opinion, and you may not want to answer this question, is it a good policy to have free governmental spending at a time like this?

Mr. McLAUGHLIN: You really want an answer?

Mr. FLEMMING: Yes, I do. I will not ask you to answer but it just seems to me that you are speaking about competing for labour; you are speaking about competing for materials; and you are speaking about competing for the various things that go with anything that pertains to development. You said money is not the final end. It is simply a commodity by which you get services, you get materials and if they are all in short supply, then you are in just about as much trouble after you get money as before. Is that right?

Mr. McLAUGHLIN: That is right.

Mr. FLEMMING: As a consequence, my question might be along this line, or at least I will make the observation, if you like, because I have no particular inhibitions about making it. It seems to me that at a time like this the withdrawal of ordinary activities by governments, municipalities if you like, and the lack of competition with private enterprise would go quite a long way toward the solution of the whole question of the tight money situation.

Mr. McLAUGHLIN: It would certainly help if the timing were right.

Mr. FLEMMING: Well, with that qualification I will not ask any more questions, Mr. McLaughlin. Thank you, Mr. Chairman.

*(Translation)*

The CHAIRMAN: Mr. Latulippe is the next one on the list, then Mr. Gilbert and Mr. Cameron.

Mr. LATULIPPE: Thank you, Mr. Chairman. In spite of all the questions which were asked in the last few days, I gather there are still some to be put, and I am sure that the representatives will answer very frankly. I would like to ask now whether the money supply is not subject to commercial operations by the bank, and is not an element the value of which is entirely based on somebody else's property?

*(English)*

Mr. McLAUGHLIN: I am afraid I did not quite get the question through the translation. It sounded as if you said the money supply is something based on other people's properties. Is that the question?



(Translation)

Mr. LATULIPPE: Yes.

(English)

Mr. McLAUGHLIN: The technical definition of money supply is made up of two things: the total deposits in the chartered banks and the amount of notes in circulation. It is just a matter of arithmetic.

(Translation)

Mr. LATULIPPE: Could you tell us who gives the necessary security when a borrower goes to a bank, whether it is the bank which gives the security or the borrower, this is what I mean by that question.

(English)

Mr. McLAUGHLIN: The guarantees? Well, the guarantee of what, Mr. Latulippe?

(Translation)

Mr. LATULIPPE: Is it the bank which secures the loan or is it the borrower who secures his loan with his own property, his real estate if you wish?

(English)

Mr. McLAUGHLIN: Whether he guarantees us with real estate? Up to now, he cannot with the banks because we cannot take mortgage security. In the future he may be able to but we make many loans secured by other than real estate and we make many unsecured loans; just the simple signing of the promise to pay. We do not always take security.

(Translation)

Mr. LATULIPPE: Thus we can conclude that the main security is provided by the borrower. Can we deduce this?

(English)

Mr. McLAUGHLIN: You see the translation came out: Can we deduct the guarantees given by the borrower?

The principal item is the signature of the borrower. The loan may or may not be secured.

(Translation)

Mr. LATULIPPE: In this case we can conclude that the bank can only charge interest on somebody else's property?

(English)

Mr. McLAUGHLIN: I do not think I get that clearly. It came out that the bank can charge interest on somebody else's property. If that is the question, the answer is, no. We charge interest on the amount of money that is borrowed, the amount of the loan. Property is probably, and up until now almost invariably, not involved at all, if you are talking of property as real estate.

(Translation)

Mr. LATULIPPE: I have been dealing with banks for the last 40 years. I have had to give 10 times the guarantee for the money I received.

(English)

Mr. McLAUGHLIN: You are dealing with the wrong bank!

(Translation)

Mr. LATULIPPE: We do not have an Imperial Bank branch there.

The CHAIRMAN: Maybe we can send a man to see Mr. Latulippe.

Mr. LATULIPPE: Could you tell us—Mr. Chairman, may I still speak, yes—could you tell us if banks are less generous in lending and more demanding for reimbursement is this not the cause of economic imbalance?

(English)

Mr. McLAUGHLIN: Would you repeat that question.

(Translation)

Mr. LATULIPPE: When the banks are not generous when they lend and they are demanding about reimbursements, does this not create economic imbalance?

(English)

Mr. McLAUGHLIN: Oh, I do not think there is an economic imbalance. By generous, there are two interpretations of that. One is whether we take a more or less credit risk or whether we are able to increase loans as much as we would like to. At the present time, we are not able to increase loans as much as we would like to, but I do not think that in the individual case, on the assessment of risks, we are any less generous. I do not think it causes any economic imbalance.

(Translation)

Mr. LATULIPPE: Would it be asking too much to enquire about the origins of this economic imbalance we have had in two World Wars. Where did it come from?

(English)

Mr. McLAUGHLIN: I am afraid we have strayed a little from Bill No. C-222, and I cannot answer that question.

(Translation)

Mr. LATULIPPE: Alright then. When there is abundant production in Canada generally and in all the economic areas, why is it the money supply is not in line with products manufactured?

(English)

Mr. McLAUGHLIN: I do not understand the translation. It says the money conforms.

(Translation)

Mr. LATULIPPE: Mr. Chairman, would you like to translate.

The CHAIRMAN: Mr. Latulippe, accept my apologies if my translation is not exact. I never studied the economic theory which is of such great interest to you. I am not sure I know your economic theory.

(English)

I think, sir, that Mr. Latulippe is trying to ask you why, if production is increasing and money is linked with goods, the money supply is not increasing along with production. How is that, Mr. Grégoire?

Mr. GRÉGOIRE: It is almost that.

The CHAIRMAN: You think there is hope for me yet.

Mr. LEBOE: You can join us almost any time.

Mr. McLAUGHLIN: Well, I think that question should be posed to an economist. I am not an economist. I like to think of myself as a practical banker.

The CHAIRMAN: Are you suggesting, sir, that economists are not practical? I understand that your bank has hired a number of them over the last few years.

Mr. McLAUGHLIN: They are very useful.

Mr. LEBOE: But not as bankers.

Mr. McLAUGHLIN: You said that, I did not.

(Translation)

The CHAIRMAN: Mr. Latulippe, the very general questions which deal with economic policy can be asked when we have Mr. Rasminsky or the professors who have tabled with the Clerk various briefs. Then we shall study these, and can discuss these general questions.

Mr. LATULIPPE: It seems to me that my questions are not very hard questions. They are very simple questions.

The CHAIRMAN: It depends which point of view is yours.

(English)

Mr. McLAUGHLIN: The questions are not very hard, but the answers are.

(Translation)

Mr. LATULIPPE: Would you be kind enough, sir, to tell us whether there is enough money supply to face the prospects for production?

(English)

Mr. McLAUGHLIN: That is a question that should be directed to Mr. Rasminsky who controls the money supply.

(Translation)

Mr. LATULIPPE: I am going to ask it in another way. Would you tell us what your rates are or how you account for imbalance between the amount of products produced and consumed?

The CHAIRMAN: I believe, Mr. Latulippe, so far as I am concerned your question seems to fall within the scope of Bill C-222. It is a general question however and we can not ask such a question of our present witness. I would like



to ask whether you could keep this question and ask the economists or the Governor of the Bank of Canada. I am sure they would be very anxious to deal with this question.

Mr. GRÉGOIRE: When these questions are put to economists it takes an hour for us to have answers and we never get them. In less than 5 minutes today, I managed to ask questions that normally would take an hour and a half. These questions, I did put to an economist, and I did not get any answers. Here with businessmen, with practical men, we get answers. This is a perfect advantage.

The CHAIRMAN: Maybe Mr. McLaughlin can give an answer in one or two minutes.

(English)

Can you give us an answer?

Mr. McLAUGHLIN: I can give an answer in less than that. Ask Mr. Rasminsky.

(Translation)

Mr. LATULIPPE: I am going to ask another question, which will be a very short question and very easy to answer, it seems to me. Would you be kind enough to tell us how is it that we owe more money than there is money?

(English)

Mr. McLAUGHLIN: Is that a personal reference?

(Translation)

Mr. LATULIPPE: I would like to proceed, Mr. Chairman. This question relates to interest rates, I believe you are very well aware of interest rates, sir, because you are certainly very well qualified, or else you would not be in the Royal Bank. Thus, I would like to ask you why there has been so much fiddling with the interest rate in the Bank of Canada since 1955? And I would like to know who really benefited from the change in interest rates, from  $1\frac{1}{2}$  to more than 6 per cent, that has taken place since 1955. If you look at the statistics for these ten years from 1955 until 1965, the banks, the stock exchange have prospered and the shares have increased while on the other hand unemployment and poverty have increased too. Who benefited from the increase in these interest rates?

The CHAIRMAN: What interest rates?

Mr. LATULIPPE: The interest rates of the Bank of Canada which were  $2\frac{1}{2}$  per cent during the war and during the recession after the war.

The CHAIRMAN: To what interest rate do you refer?

Mr. LATULIPPE: The interest rates of the Bank of Canada have increased from 2 per cent to 6 per cent. I wonder why these rates have been increased and who benefited from this? This, of course, stepped up other rates and then, the debentures went up from  $2\frac{1}{2}$  and 3 per cent to  $4\frac{1}{2}$  per cent. Who benefited from these increases in the interest rates? Was it the Bank of Canada or chartered, or private persons who benefited? Who profited by all this?

(English)

Mr. McLAUGHLIN: The first part of your question I think had to do with fiddling with interest rates by the Bank of Canada. I come back to the same answer almost as I gave to your previous questions. I think you had better ask the fiddler. That is your answer.

The CHAIRMAN: But remember he who pays the fiddler calls the tune.

(Translation)

Mr. LATULIPPE: Could you please tell us despite all this playing about with the interest rates, why the rate of the chartered banks remained at 6 per cent. This contributed, it seems to me, to maintain some stability in credit at the popular level, at the level of the ordinary persons and in business transactions, in industrial transactions. What will happen if we drop this ceiling now at 6 per cent, what will happen if we abandon this rate as is requested in the bill. Will this be good for the people or not?

(English)

Mr. McLAUGHLIN: It will certainly be good for the country.

Mr. LATULIPPE: For the banks.

Mr. McLAUGHLIN: Not necessarily.

(Translation)

Mr. LATULIPPE: Now, Mr. Chairman, if the increase in interest rates does not contribute to the increase in the cost of living, could you tell us whether the increase in wages contributes to increasing the cost of living?

The CHAIRMAN: Our discussion is not on increases in the cost of labour, which is a general matter. We are discussing banking policy, if you are going to put questions on the interest rates, I can allow them. This is the sort of question the witness will attempt to reply to, but questions of wages are a good deal too broad.

Mr. LATULIPPE: It seems to me that labour cost has helped to increase the cost of living, if you increase the interest rates you will increase the cost of living and it will be still more difficult for ordinary citizens to meet their costs. The interest rates will increase the cost of living.

The CHAIRMAN: We must ask the witness then, whether he is in agreement with you about this, that's your question, is it not? Is that your question?

Mr. LATULIPPE: I think it's a question which is an elementary one, if the witness does not want to reply, obviously I can't oblige him to reply it.

(English)

Mr. McLAUGHLIN: It is not that I do not want to reply. It is just that I am a simple banker trying to operate the Royal Bank of Canada at a profit, and you are asking me questions that should properly be posed to an economist. I cannot answer them.

The CHAIRMAN: I never knew there was such a—

(Translation)

Mr. LATULIPPE: I agree with you that you represent the Royal Bank, you represent the Association of Bankers and you will understand with me that we represent the people, and our responsibility and our duties are to see to the interests of the public while protecting the interests of the banks. We feel we need the banks. They are good institutions. We must keep them. They are institutions in which there are tremendous transactions conducted that benefit the whole country. But I want to know if there would be an improvement in the financial picture, if there would be an improvement for the chartered banks and in the general economic standing of the people. You know there are a good many people who do not live decently, who do not live at a standard in line with the standard of the living of the country.

The CHAIRMAN: Are you putting a question to the witness or are you making a statement?

(English)

Mr. McLAUGHLIN: I will agree with you that the banks are good institutions.

(Translation)

The CHAIRMAN: I am sorry, Mr. Latulippe, but your period for putting questions has come to an end. You have had more than twenty minutes. We now have seven minutes and I will ask the Committee what is your desire, do you want to sit this evening? On my list there are the names of Mr. Gilbert and Mr. Cameron. As there is no other person to put questions, would the Committee want to stay here for a few minutes after 6 o'clock and if there are any others who want to put questions?

(English)

Are there others who have questions in mind? Perhaps it would be useful then, rather than schedule a session for tonight, if the witness would be available for a few minutes past six o'clock.

Mr. McLAUGHLIN: It is quite agreeable with me.

The CHAIRMAN: We could have the question of Mr. Cameron and Mr. Gilbert and then we would try and—

Mr. GRÉGOIRE: Who will be our witnesses on Thursday?

The CHAIRMAN: Well, that is a very interesting problem which I have been working throughout the afternoon to try and resolve.

Mr. GRÉGOIRE: Could we have the Minister?

The CHAIRMAN: Well, we are going to look into that. These suggestions have been made and I just want to repeat that up to now the consensus has been, and may have changed, that we call the Minister before us to discuss with him and question him at length. Not only on the legislation itself but on the points raised by all the witnesses once they have been before us. There may be some change of view on that.

We are having a steering committee meeting tomorrow at noon. I do not suggest that we try to solve this problem here but I can assure the Committee that I have asked the Clerk to canvass very thoroughly those who might be able



to come here, bearing in mind the need of the Committee to have an opportunity to study their briefs before they appear. It is not just a matter of using the time; it is also a matter of the Committee being in a position to place questions before the witnesses which will be based on some study of the issues the witnesses have in mind.

I am not sure which of you gentlemen wish to begin. Mr. Gilbert.

Mr. GILBERT: Mr. Chairman, I am very pleased that Mr. McLaughlin describes himself as a practical banker because I am going to put three questions to him that were dealt with by the Porter Commission and ask for his comments on them.

The first was the recommendation by the Porter Commission that there should be a statutory prohibition on charges for negotiation of out of town cheques, the actual handling of which does not involve any significant cost to institutions concerned. What do you think of that recommendation, Mr. McLaughlin?

Mr. McLAUGHLIN: May I read to you something I said when I first made public comment on this. I am quoting from a speech I made in Winnipeg on June 10, 1964.

Two other relatively minor recommendations of the Commission deserve at least passing notice. The first is the recommendation that charges for the negotiation of out of town cheques should be prohibited. It seems to me that in this instance the Commission delved rather deeply into what are purely administrative matters of the banks. The recommendation is not new. The Macmillan Commission which reported in 1933 made the same suggestion but stated "it should be understood, however, that this change would involve the postponement of credit dating to correspond with the time necessary to encash the cheque."

In this way the Macmillan report recognized that there is a cost involved in clearing these cheques. Although exchange is not charged in the United States, cost is recovered by value dating deposits, i.e. the deposit of a cheque on another centre would not receive credit until the item had been cleared. The Canadian custom is to give immediate credit and to recover costs by making a direct charge. I suggest that this is purely an administrative problem for the banks.

The CHAIRMAN: It is also an expense to the public.

Mr. McLAUGHLIN: And an expense to the banks.

The CHAIRMAN: And to the banks. How do you draw a distinction between administrative problems of the banks and all the other things we have been talking about, interest rates, concentration of ownership, and so on. In view of the fact that the banks are under federal jurisdiction and there is a very comprehensive statute, is there any matter that the banks deal with that is purely administrative that cannot be looked at by his Committee or parliament?

Mr. McLAUGHLIN: Oh, not at all. I was not suggesting that.

Mr. GILBERT: Thanks, Mr. Chairman. I think also in Europe there is no charge for cashing out of town cheques.

Mr. McLAUGHLIN: I never cashed a cheque in Europe. I do not know.

Mr. GILBERT: Well, this is what the report says and you are passing on to the Committee that there is no charge in the States and I was just interjecting.

Mr. McLAUGHLIN: Is there value dating in Europe?

Mr. GILBERT: I really do not know. But that is your reason of objecting to it.

The second question is with regard to the recommendation of the cheque clearing facilities. The Porter Commission recommended that the cheque clearing facilities be under the control of the Bank of Canada rather than under the Canadian Bankers' Association the way it is now. What are your views on that, sir?

Mr. McLAUGHLIN: They are no different than the views of the Canadian Bankers' Association which have been expressed previously on this question.

Mr. GILBERT: Well, offhand, are they for it or against it? I cannot recall at the moment.

Mr. McLAUGHLIN: They do not think it would accomplish anything.

The CHAIRMAN: You are referring to what recommendation specifically, that the clearing be handled by the central bank?

Mr. GILBERT: By the central bank rather than by the Canadian Bankers' Association.

The CHAIRMAN: The Bankers' Association were very much in favour of maintaining the present system.

Mr. GILBERT: And you agree with that? What is your reason for saying that, Mr. McLaughlin?

Mr. McLAUGHLIN: I cannot see any advantage to the Bank of Canada on that account.

Mr. GILBERT: Now, the third question is with regard to bank charges. You will note that there is no definition of bank charges in the Bank Act. With regard to consumers' loans, a recommendation of the Porter Commission was that all charges should be clearly defined and represented on a percentage basis with regard to the cost of loans. Would you be in favour of that?

Mr. McLAUGHLIN: I have no objection whatsoever. We have nothing to hide. I would hope that others would have to do it, too. My only provision is that you set out an arithmetically possible method of doing it, but in principle I have no objection.

Mr. GILBERT: You notice that the Small Loans Act that has the definition "cost of loan" sets forth what constitutes the cost of the loan. Do you think the definition contained in the Small Loans Act would be applicable to a consumer's loan in the—

Mr. McLAUGHLIN: I am sorry, I do not know that definition. We do not operate under that act and I am not familiar with the definition.

Mr. GILBERT: Well, when a person signs an application for a consumer loan are the charges set forth in that application? In other words, there is the cost of the loan, together with that. Is there a statement of what he may be charged with?

Mr. McLAUGHLIN: He certainly knows the total cost. I do not know whether he knows it converted into a per cent because there are I think six different ways of doing it, but you just tell us the way that it is arithmetically possible and simple and we have no objection to doing it that way.

Mr. GILBERT: Thanks, Mr. Chairman. That is all.

The CHAIRMAN: Mr. Cameron, and I believe—

Mr. MONTEITH: I have one very closely related question, Mr. Cameron, if I could interject it now. In your opinion, Mr. McLaughlin, would it be legal to inform a customer that as a surcharge he will in future keep a free balance of at least ten per cent of his borrowings, or pay an extra 6 per cent on 10 per cent of his borrowings? I said he is told that this is in lieu of a surcharge.

Mr. McLAUGHLIN: I do not know. I have never done so. I have never had to refer to legal counsel whether it was legal or not.

The CHAIRMAN: Are you referring to an instance that has been reported to you, if I may be so bold?

Mr. MONTEITH: Yes. Quite. That is all.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): A little while ago you were asked and gave a very forthright answer with regard to your view about the foreign ownership of Canadian banks. I happen to share your view but I have an uneasy feeling that my opinion may be largely subjective and perhaps emotional and I was wondering if you could give me some objective reasons why you object to the foreign ownership of Canadian banks.

Mr. McLAUGHLIN: I think the best way I can answer that question, Mr. Cameron, is to say that over the years there have been a number of reasons advanced by a number of people as to why control of our major financial institutions should remain in Canadian hands. There are dozens of reasons given by dozens of people. I just think I agree.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You cannot be more specific than that.

Mr. McLAUGHLIN: No.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well, in view of your, shall I say, quite decided opinion on this which I happen to share, what course do you think should be followed with regard to the Canadian bank that is now wholly owned by a foreign bank.

Mr. McLAUGHLIN: That is a diplomatic question now.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Do you think there might be some value in the act being amended to enable the Canadian government, if it decided it was in the interest of the country, to take that bank over?

Mr. McLAUGHLIN: I would not want to see the government take the bank over, no.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Now, why would you not?

Mr. McLAUGHLIN: I am a believer in private enterprise.



Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You know, of course, that there are countries too that are very similar to ourselves, even in Australia, where the major commercial bank of the country is a public institution.

Mr. McLAUGHLIN: Well, in Australia it was the central bank which also did commercial business.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It started as a commercial bank, Mr. McLaughlin.

Mr. McLAUGHLIN: It is being separated now.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It was later established also as a central bank, but it is the largest commercial bank in Australia.

Mr. McLAUGHLIN: The Bank of England also does a little private business, too.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes. Do you think this has a deleterious effect on the economy?

Mr. McLAUGHLIN: I just do not happen to like it.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Your own peculiar subjective views.

I have another question, Mr. McLaughlin, I am sure you like almost everybody else has been rather disturbed by the difficulties into which some financial institutions have been finding themselves recently. Only today one went into bankruptcy.

The question I would like to ask is this. Although, looking at the profit accounts of the chartered banks I am a little hesitant to let them have any more freedom in the jungle. Nevertheless, is there any way do you suppose by which the chartered banks could be put in the position of performing the function, if there were useful functions for these institutions which have rather rocked the financial world of Canada, of those sorts of institutions?

Mr. McLAUGHLIN: I think that had the 6 per cent ceiling not been on the banks in the last ten years, and as interest rates went up gradually, the so-called near banks would not have grown to the extent that they have. They would have existed and they would have grown but they would not have sprung up quite that fast, and you might not have had some of them get out on a limb so far. But you cannot legislate against gullibility, if people want to get 10 per cent when that is far above the going rate. They got the 10 per cent for a while but maybe they lost the principal and I do not know how you can legislate against gullibility.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But can you not legislate against the capacity to take advantage of people's gullibility.

Mr. McLAUGHLIN: Well, that is a pretty tall order.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): After all we have a great deal of legislation that does purport to protect people from their own gullibility.

Mr. McLAUGHLIN: That is right.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You see what I have in mind is there any extension of the powers of the banks beyond the one you

mentioned, the interest rates, that would be required to perform these sorts of functions, and I must confess I am rather vague as to what operations the Prudential, the Atlantic and the Laurentide did engage in. I know the Laurentide was a type of a small loan company because I happen to know the people who were running it, but as to the others I am a little vague as to what they did engage in. Are there any of the things that they engaged in that were legitimate and valuable that banks could have done?

Mr. McLAUGHLIN: I think with respect to one of them that is under investigation they are taking a long time to find out what they did engage in.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): That is what occurred to me.

Mr. McLAUGHLIN: I cannot think offhand other than, as I said before, the hampering effect of the 6 per cent ceiling has slowed down the growth of the banks, not absolutely but relatively, and that some of these near banks under practically no control have grown up overnight without supervision. I do not think that would have happened had we not been under the legislative inhibitions of the 6 per cent ceiling.

Mr. CLERMONT: Mr. Cameron, would you allow me a supplementary?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, of course.

Mr. CLERMONT: Do you think too that besides the 6 per cent ceiling, Mr. McLaughlin, that a better supervision of these companies would have helped, too?

Mr. McLAUGHLIN: Absolutely. I quite agree.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well, this is the basis of my next question. Do you think it worth while this Committee exploring the possibilities of legislation that will bring such institutions under federal control and sanction.

Mr. McLAUGHLIN: Provided you can overcome the constitutional problems. Most of them have provincial charters.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I know. It all hinges again on the question that Mr. Lambert is always raising, the definition of banking, of course. Do you think it would be worth while if we could come up with a definition of banking that would bring them under the umbrella, that it would be worth trying to do it?

Mr. McLAUGHLIN: I think it would be an interesting experiment, but I think you realize that you will raise up an horrendous constitutional problem that will—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well, we have had horrendous constitutional problems before.

The CHAIRMAN: And sometimes horrendous results!

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well, not too horrendous.

(Translation)

Mr. LATULIPPE: Mr. Chairman, a supplementary question?

The CHAIRMAN: Yes, Mr. Latulippe.

Mr. LATULIPPE: Could Mr. McLaughlin please tell us—he said a minute ago that he does not like nationalization of banks—credit would be nationalized for the public good?

The CHAIRMAN: To be fair to the witness, we cannot go into the area of economic policy in its broader sense. If Mr. McLaughlin wants to attempt an answer, I will not stop him, but I think that this is a pretty broad and hypothetical question in the field of economics. You will only get an answer along the line of your question; it would be a very broad answer, that is all.

(English)

Mr. McLAUGHLIN: Mr. Chairman, you do not need to try to stop me. I cannot even get started.

The CHAIRMAN: I think Mr. Monteith had a question.

Mr. MONTEITH: Just one question. Mr. McLaughlin, this morning we were discussing RoyNat and the fact that it was incorporated about four years ago.

Mr. McLAUGHLIN: Nineteen sixty one.

Mr. MONTEITH: And you are objecting to the clause in the bill before us which is retroactive to the effect that it is presumably going to affect your interest in RoyNat if it goes through in the form it is now.

Mr. McLAUGHLIN: That is right.

Mr. MONTEITH: Well, then, would you not agree that any retroactivity concerning legislation having to do with the Mercantile Bank which was incorporated in 1953, and according to the laws of the country at that time would not be good principle?

Mr. McLAUGHLIN: Well, let me go back to RoyNat for a minute. One of the reasons I mentioned before my plea was retroactivity, but as the discussion developed I was able to bring out the fact that I would like to see an enabling clause somewhere in the bill so that if a gap existed in the future another type of company could be formed by a group of banks, trust companies or something of that order to fill that gap. I was making a plea not only retroactive but for the future. So I do not want you to hang too much on the retroactivity of it. That is one reason I would like to see an opening for—

Mr. MONTEITH: Well, you certainly do not think that your present set up should be disturbed, though?

Mr. McLAUGHLIN: That is right.

Mr. MONTEITH: Well, does it seem logical to be retroactive concerning the Mercantile Bank then?

Mr. McLAUGHLIN: Mr. Monteith, this question has got into the realm of diplomacy.

Mr. MONTEITH: Oh, I think it is an honourable situation. We have to deal with it?

Mr. McLAUGHLIN: I do not think that the Mercantile Bank is going to put the other banks out of business.



The CHAIRMAN: When you refer to the desirability of Canadian banks remaining under Canadian control, would you include the Mercantile Bank and their being under Canadian control?

Mr. McLAUGHLIN: I think we have to accept a given situation and start afresh from there, but do not forget that at the same time I made a plea for foreign banks to be able to enter Canada.

The CHAIRMAN: An agency, yes.

Mr. McLAUGHLIN: I do not want this to be exclusively a Canadian bank preserve.

Mr. CLERMONT: A supplementary, Mr. Chairman. How many states will allow outside banks to come within their limits?

Mr. McLAUGHLIN: I do not know. There are some that will not, Illinois will not allow them. There are a number that will not. I do not know that anybody has ever investigated them because there are some states in the middle of the United States where there is just no volume of Canadian business. I do not think anybody has looked into it.

Mr. CLERMONT: Out of the 50 states, will we find 10 states that will allow foreign capital?

Mr. McLAUGHLIN: I do not know.

Mr. MONTEITH: You will find a state as big as Canada that does. New York.

Mr. CLERMONT: Yes, but Mr. Monteith I am asking the question of Mr. McLaughlin.

Mr. McLAUGHLIN: I do not know. I have never seen any research on that.

The CHAIRMAN: Well, I think we have exhausted our questions.

I would like to thank Mr. McLaughlin for very useful answers, to a vast range of questions. We are happy to have all our witnesses before us and I will inform the Committee as soon as possible about the business for Thursday. I remind members of the steering committee present about our luncheon meeting tomorrow.

Mr. MONTEITH: Twelve thirty, is it?

The CHAIRMAN: One o'clock. That will give us time to finish our caucus and go on. Until Thursday, therefore, I declare this meeting adjourned.

## APPENDIX "T"

OTTAWA 4, November 29, 1966.

Memo to Mr. Clermont

From M. R. Prentis

*Bank Service Charges*

I attach a schedule setting forth some of the charges made by banks in the U.S. and Canada for the more frequent entries in clients' accounts. The information available is sketchy and there are blanks in this schedule. However, the detail presented is sufficient to suggest that charges on these items are in general rather lower in the U.S. than Canada, although the more extensive use in the U.S. of a standing monthly charge for operating the account ("maintenance fee") offsets this advantage as far as the vast majority of accounts—the relatively small ones—is concerned.

It is noteworthy that there is a wide range of charges for the same service as between banks in the U.S., and even as between banks in the same city. In Canada, by contrast, the charges for the basic services shown are the same in all the banks. In the U.S., there is evidence that the costs of making the various entries now substantially exceed the corresponding charges made, and some general upward adjustment could well occur in course of time. In Canada the charges are probably a little more realistic, although this cannot be proved by means of any material available to us.

The method used by the Canadian banks to meet rising costs has reflected the wide degree of discretion enjoyed by managers. Thus, whereas a few years ago many services were often not charged for, the charges are now as a rule meticulously applied. More particularly, however, the manager's discretion has been applied increasingly in the bank's favour in setting charges for services not listed: drafts, transfers, foreign exchange dealings, travellers' cheques, collections and many of the other services provided by banks. The practice of requiring clients to maintain a minimum balance in their deposit accounts has also become widespread. Typically, interest is paid on these balances, but (as the Porter Report indicates) the cost of funds to the banks is well below the rates charged on loans, so that the banks have been able to improve their financial position vis-à-vis their clients by this means.

Much may be said for and against the concept of "compensating balances". However, it is of interest that this practice has become more widespread in Canada at a time when many bankers in the U.S. are considering the desirability of abandoning it in favour of realistic pricing of services.

Some charges for specific services are set out in the draft legislation, in clauses 91 and 92. Clause 92 is the provision under which banks charge exchange on out-of-town cheques.

RATES OF CHARGES MADE BY BANKS FOR SPECIFIED SERVICES  
U.S. AND CANADA

Service	Canada (1966)			U.S.A.		
	1955			1963		
	Current Account	Savings Account	Pers. Chg. Account	Current Account	Savings Account	Pers. Chg. Account
Deposits credited, drawn "on us",.....	10¢	—	—	3¢ to 5¢	—	—
drawn on others.....	14¢	—	—	4¢ to 5¢	—	—
Currency deposited.....	95¢ per \$M	—	—	5¢	—	—
Coin deposited.....	\$1.80 per \$C	—	—	5¢	—	—
Cheques debited.....	10¢	15¢	10¢	5¢ to 10¢	4¢ to 20¢	5¢
Items returned NSF.....	\$1.00	\$1.00	\$1.00	50¢ to \$2.00	50¢ to \$2.00	10¢ to 25¢
Maintenance fee.....	*	—	—	0 to \$1.00	25¢	75¢
Overdraft.....	?	—	—	50¢ to \$2.00	—	—
Certification.....	—	—	—	25¢ to 50¢	—	—

\* Calculated on analysis sheet, which allows 3% interest (annual rate) on average balance in the account.



## APPENDIX "U"

November 29, 1966.

## MEMO

To: Mr. G. Clermont M.P.

From: Denis Baribeau B. Com., M.A.

Subject: Instruments eligible for re-discount at Federal Reserve Banks

1. The United States Federal Reserve System is composed of 12 Federal Reserve Banks under the responsibility of a Board of Governors composed of seven members.

2. In the United States, a bank can be licensed by the State or the Federal government. If Federally chartered, a bank is said to be a national bank and must be a member of a Federal Reserve Bank, that is, it must own stock of a Federal Reserve Bank. A State bank may also be a member bank if it agrees to conform to requirements set up for member banks.

3. A member bank can borrow from its Federal Reserve Bank. The borrowing can take place in two main ways:

- rediscounting eligible paper
- getting advances by pledging collateral

(A) *Rediscounting eligible paper*

In rediscounting, a member bank endorses a paper (IOU's received from its borrowers) which must meet FR standards of eligibility and sends it to the "Fed". The latter then deduct interest (discount) and credits the member bank's account with the *remainder*.

Today, the criteria of eligibility for rediscount still reflect pre-1914 thinking that bank lending should be concerned with self-liquidating commercial loans. This thinking in fact limits eligibility to notes, drafts, or bills of exchange maturing within ninety days (nine months in case of agriculture loans) and given to banks in order to finance production and the distribution of goods and include also notes given to banks for the purpose of buying United States government securities.

Rediscounting has lost popularity in the United States and the more common method of borrowing today is to get direct advances from the "Fed" by pledging acceptable collateral.

(B) *Advances*

Direct advances, usually for fifteen days, is the more common practice today through which a member bank can borrow from the "Fed". The member bank must in return give its own note *supported by collateral to at least the amount borrowed*. The collateral may be commercial paper meeting standards of eligibility for discount (short term paper).

Most often the securities pledged are government bonds. Often, the securities pledged are those which the member bank has before hand asked the Federal Reserve to hold for safekeeping.

An interesting point worth noting here is that in the U.S., Congress has given the Federal Reserve authority to accept other types of collateral satisfying the FR. An example of such collateral are "notes pledging term loans". When such assets are used by the member bank with the FR consent, a penalty interest charge equal to 1/2 percentage point above the rate on other borrowing is charged. This penalty rate is a fossil coming from the pre-first world war thinking.

This last case is interesting for Canada since the banks will now be permitted to enter the conventional mortgage lending field. Should such mortgage notes be eligible as collateral for advances from the Bank of Canada?

## APPENDIX "V"

## SUBMISSION

to the

HOUSE OF COMMONS STANDING COMMITTEE

on

FINANCE, TRADE AND ECONOMIC AFFAIRS

OCTOBER 1966

THE ROYAL BANK OF CANADA

W. EARLE McLAUGHLIN

CHAIRMAN AND PRESIDENT

1. I welcome this opportunity to make a Submission to the Committee on Finance, Trade, and Economic Affairs, in order to express my views on the one aspect of Bill C-222 which relates directly to The Royal Bank of Canada, of which I am the Chairman and President, and to one other chartered bank—the Banque Canadienne Nationale. I am pleased to say that Mr. Louis Hébert, President of the Banque Canadienne Nationale, supports this presentation.

2. Section 76(1) of Bill C-222 requires both The Royal Bank of Canada and the Banque Canadienne Nationale to reduce their voting stock interest in a Canadian corporation, RoyNat Ltd., of which they were the main founding shareholders and of which they are still the main shareholders. By the terms of this section each bank must reduce its voting stock interest in RoyNat to 10 per cent by July 1, 1971. In section 76(7), the Bill does provide for two exceptions—a "bank service corporation" and the Export Finance Corporation of Canada Ltd. It is not clear, however, from the definitions in section 76(8) that RoyNat would be eligible for exemption as a bank service corporation. In this Submission, therefore, I wish to put before you the case for explicitly exempting RoyNat from the provisions of section 76 of the Bill C-222.

## THE BACKGROUND

3. Before I make that case, let me give you some facts about RoyNat.

4. RoyNat was incorporated in the early part of 1962, although the idea behind RoyNat had been under consideration for a number of years before the final decision to go ahead was made in 1961 when the demand for the type of facilities it would offer became increasingly evident. The purpose of RoyNat is to provide term financing to medium-sized Canadian business firms; that is, firms too large to take advantage of the Small Business Loans Act but not large enough to go to the capital market. It does not provide financing for pure real-estate investment and land development purposes.

5. The growing volume of business being done by the Industrial Development Bank (considerably exceeding in some ways the scope contemplated when it was chartered) attests to the unfilled need for further private sources of term



financing for medium-sized businesses. Accordingly, two chartered banks and three trust companies subscribed a total of \$10 million to provide the paid-up capital for RoyNat. Today the Royal Bank holds 41.5 per cent of the stock, and the Banque Canadienne Nationale holds 34.0 per cent.

6. Setting up RoyNat was the only way the two chartered banks could fill the financial gap that seemed to exist in the economy. RoyNat, not being in a position to take direct mortgage security, finances its clients mainly through the acquisition of debentures or bonds or both, and charges rates commensurate with its cost of funds and overhead. This could not be done by the chartered banks under the existing (1954) Bank Act. The banks were legally forbidden both to take mortgage security and to charge the market rate for this type of term loans because it was higher than the legal maximum interest rate of 6 per cent. But, above all, RoyNat can borrow at long term in the capital market, as an organization that lends at long term should do. To date, RoyNat has borrowed \$75 million from the public on a longterm basis. It very seldom borrows from its bankers, and then only in modest amounts and, on each occasion, only for a few days at a time.

7. And what has RoyNat accomplished? In the approximately four and a half years in which RoyNat has been in existence, it has made loans of over \$100 million, a clear indication of the need that exists for term-financing facilities designed for medium-sized business. RoyNat's clients, past and present, include 655 companies employing well over 30,000 people. In particular, RoyNat has assisted in the establishment of 64 new companies and has financed the purchase, by Canadians, of 37 other companies.

8. RoyNat makes its facilities available to everyone on the same terms and conditions, regardless of the borrower's banking affiliation. Thus, about 200 of RoyNat's borrowers are not clients of RoyNat's two banking shareholders.

9. On a regional basis, approximately 7 per cent of RoyNat's customers are located in the Atlantic Provinces, 44 per cent in Quebec, 19 per cent in Ontario, 11 per cent in the Prairie Provinces, and another 19 per cent in British Columbia. The high percentage of customers in Quebec reflects the fact that RoyNat's head office is in Quebec and a preponderance of its early business came from that province; however, RoyNat's business in other parts of Canada is steadily growing.

10. To carry out its functions, RoyNat has built up a staff of highly trained individuals now numbering 100 (of which 44 are bilingual), located in seven district offices across Canada. Among them they represent the wide variety of professional background necessary for the proper assessment of the term-financing requirements of Canadian business.

11. In addition to its own offices, RoyNat, through the branches of its banking shareholders, is able to provide ready access to its facilities in all areas of Canada. At the end of September, 1966, the banking shareholders of RoyNat had over 1700 branches in Canada; and these automatically provide doorways to RoyNat facilities in virtually every community, large and small, throughout the country.

12. RoyNat has been most successful in building up a nation-wide lending facility, nevertheless to date its profits have been modest. It has competed

successfully with mortgage companies, finance companies, private development companies, foreign investors, and miscellaneous federal and provincial government agencies, including the Industrial Development Bank. These last-named competitors often lend at rates below the market, pay no income taxes, and are otherwise indirectly subsidized in their operation. The net profit for RoyNat's four fiscal years to date, after paying taxes of \$747,500, amounts to a grand total of less than \$1 million, or less than 10 per cent on paid-up capital—an average annual rate of return of only  $2\frac{1}{2}$  per cent per year. Thus, the founding shareholders have yet to gain an adequate rate of return on their investment: the same amount invested in government bonds over the same period would have earned substantially more. As with any relatively young enterprise, it will take time before the shareholders can expect to receive a reasonable return on their venture capital. In the meantime they are providing, through RoyNat, a valuable service to the Canadian economy.

13. Nevertheless, if section 76 of Bill C-222 is applied to RoyNat, both the Royal Bank and the Banque Canadienne Nationale will have to reduce their investment in RoyNat: by about 75 per cent for the Royal and by about 70 per cent for the Banque Canadienne Nationale.

#### THE CASE FOR EXEMPTING ROYNAT FROM SECTION 76 OF BILL C-222

14. My case against forcing these two banks to divest themselves of so much of their ownership is as follows:

(a) The proposed legislation is retroactive. A need clearly existed, and still exists, for the type of services now provided by RoyNat. The owners of RoyNat saw this gap in the private sector of our financial system and stepped in to fill it. Proof of the need is evidenced by the volume of loans RoyNat has made. It is a credit to the initiative of the two banks, The Royal Bank of Canada and the Banque Canadienne Nationale, that they, while competing keenly for normal banking business, have made a joint effort with three trust companies to create a type of lending business which, though needed, could not have been set up by any of the institutions working alone.

(b) To stifle initiative by retroactive legislation is wrong in principle and unfair to those it affects. To stifle future initiative—directed towards other gaps in our financial system that may in time appear—seems equally unfair, and certainly contrary to the public interest. The Porter Report itself, with remarkable foresight in view of section 76 of Bill C-222, makes this very point as follows:

... we would not wish to see the legislation inhibit useful innovations and improvements in the financial system by preventing or unduly restricting the participation of banking institutions in new joint ventures with other businesses or with other members of the financial community. In situations of this kind, of which there have been a few recently, Treasury Board approval might be almost automatically forthcoming provided that the institution concerned has less than a controlling interest (p. 371).

(c) The Export Finance Corporation Ltd., now exempt under Section 76(7) of Bill C-222, is owned by all the banks with no bank in a position of control. RoyNat is owned by two banks and three trust companies with no bank or trust company shareholder in a position of control. It would seem, therefore, that RoyNat should be exempt under the same principle that appears to be applied to the Export Finance Corporation Ltd.

(d) The Porter Report, in a specific reference to RoyNat, points out the advantages of a corporate entity in this specialized field, as follows:

The need for specialized lending skills in dealing with small business financing was one of the reasons which led two chartered banks and three trust companies to join forces in 1962 to establish a subsidiary company, RoyNat Ltd., to provide "expanding and new Canadian businesses with financing beyond the normal scope of banking facilities." Through this company, the partners are able to combine the advantages of their extensive branch systems, the source of much business, with a specialized staff of bankers, accountants, engineers, lawyers and others in six [now 7] offices across the country. The company is also free...to charge rates above 6 per cent which are appropriate to its business...The company has some equity investments but participations are relatively small, control is avoided and directors are not appointed to borrowers' boards (p. 225).

On the basis of this reasoning, along with that in (b) above, it would appear that the Porter Commission would certainly exempt RoyNat from its recommendation that, in general, banks should not own more than 10 per cent of another financial corporation.

15. Most of the advantages to RoyNat of having a close association with two chartered banks would be lost if each of the banks had to reduce its investment to 10 per cent of the total. Specifically these advantages are as follows:

(a) RoyNat would have to charge higher interest rates because RoyNat exists on the spread between what it charges and what it pays. The two banks do not guarantee its long-term borrowings from the public but the moral backing of the banks, as evidenced by their present ownership and sponsorship, is sufficient, I am satisfied, to enable it to raise its money from the public at less than it would otherwise have to pay. When the ownership of the two banks is reduced to the nominal proportions now proposed in Bill C-222, this sponsorship in the minds of the investing public would evaporate and RoyNat could be forced to pay more than it does now for its long-term borrowings. This in turn means higher rates of interest on the loans it grants.

(b) The association of The Royal Bank of Canada, the Banque Canadienne Nationale, and the three trust companies in a Canada-wide corporation has in itself a cohesive value for Canada that could be lost if RoyNat shares were sold to others. In addition this association with its five shareholders gives RoyNat an opportunity to provide its clients with useful services that go beyond the mere making of loans.

(c) The public would be deprived of the ready access to information concerning RoyNat's facilities through the more than 1700 branches of the



two banks located in virtually every community in Canada; and RoyNat itself would be forced to incur considerably higher costs in replacing these sources of inquiries concerning term lending propositions in so many communities. In fact RoyNat as it exists is indeed unique in having so many contact points to act as entrées to its services. For example, 57 per cent of all the inquiries received by RoyNat emanate from branches of the two banking shareholders.

16. In short, while RoyNat would no doubt be able to carry on without a close association with its bank sponsors, it could not carry on as effectively or as economically. And I submit that the fate of RoyNat is of some concern to this Committee. The consequences of forcing the two banks to loosen their ties with RoyNat are as follows:

(a) The RoyNat type of operation cannot be readily duplicated or carried on by a chartered bank acting alone. Most banks do not have the specialized organization, or the specialists, necessary for this type of financing. Furthermore, banks cannot borrow long to the same extent that RoyNat can, and short-term borrowing for long-term financing is unsound financial practice. Finally, it is doubtful if banks, to the extent that they will be able to move into term financing under the provisions of Bill C-222, will be interested in moving into the medium-size business field now serviced by RoyNat.

(b) If the two banks are forced to divest themselves of all holdings over 10 per cent, it is difficult at this point to predict precisely what the result will be in terms of diversification of ownership. Obviously, ownership might, at least initially, become much more widespread. But no matter what methods are used to accomplish the divestment of bank-owned shares, there would be no guarantee that the new ownership would remain widely diversified. In fact, given RoyNat's growth potential, based on the growing need for its services, it is likely that a single outside interest might attempt successfully to gain control. If this happened to be a foreign interest, and there is no reason in law or economics why it should not be, we should have another example of a Canadian financial corporation falling needlessly out of Canadian control.

### CONCLUSION

17. I submit, therefore, that both for reasons of principle and for highly practical reasons as well, Bill C-222 should be amended so as to add the name "RoyNat Ltd." after the name "Export Finance Corporation of Canada Ltd." in section 76(7).



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LÉON-J. RAYMOND,  
*The Clerk of the House.*



HOUSE OF COMMONS  
First Session—Twenty-seventh Parliament  
1966

STANDING COMMITTEE

ON

FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. HERB GRAY

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MINUTES OF PROCEEDINGS AND EVIDENCE

No. 30

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THURSDAY, DECEMBER 8, 1966

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Respecting

Bill S-30—An Act to incorporate League Savings  
and Mortgage Company.

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WITNESSES:

Messrs. D. Gordon Blair, Parliamentary Agent; R. D. MacMullin, Managing Director, Nova Scotia Credit Union League; H. R. MacEwan, M.P., Sponsor of Bill S-30; R. Humphrys, Superintendent of Insurance.

ROGER DUHAMEL, F.R.S.C.  
QUEEN'S PRINTER AND CONTROLLER OF STATIONERY  
OTTAWA, 1966

STANDING COMMITTEE  
ON  
FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. Herb Gray

*Vice-Chairman:* Mr. Ovide Laflamme

and Messrs.

Addison,  
Basford,  
Cameron (*Nanaimo-  
Cowichan-The Islands*),  
Cashin,  
Chrétien,  
Clermont,  
Coates,

Comtois,  
Flemming,  
Fulton,  
Gilbert,  
Irvine,  
Johnston,\*  
Lambert,  
Lamontagne,  
Latulippe

Leboe,  
Lind,  
McLean (*Charlotte*),  
Monteith,  
More (*Regina City*),  
Munro,  
Valade,  
Wahn—(25).

Dorothy F. Ballantine,  
*Clerk of the Committee.*

ORDER OF REFERENCE.

THURSDAY, December 1, 1966.

*Ordered*,—That Bill S-30, an Act to incorporate League Savings and Mortgage Company, be referred to the Standing Committee on Finance, Trade and Economic Affairs.

Attest.

LÉON-J. RAYMOND,  
*The Clerk of the House of Commons.*



## REPORT TO THE HOUSE

DECEMBER 9, 1966.

The Standing Committee on Finance, Trade and Economic Affairs has the honour to present its

### SEVENTEENTH REPORT

Your Committee has considered Bill S-30, An Act to incorporate League Savings and Mortgage Company, and has agreed to report it without amendment.

Respectfully submitted,

HERB GRAY,  
*Chairman.*

## MINUTES OF PROCEEDINGS

THURSDAY, December 8, 1966.  
(59)

The Standing Committee on Finance, Trade and Economic Affairs met at 11.10 a.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Addison, Cameron (Nanaimo-Cowichan-The Island), Chrétien, Comtois, Flemming, Fulton, Gilbert, Gray, Lambert, Latulippe, McLean (Charlotte), Monteith, Wahn—(13).

*In attendance:* Messrs. D. Gordon Blair, Parliamentary Agent; R. D. MacMullin, Managing Director, Nova Scotia Credit Union League; H. R. MacEwan, M.P., Sponsor of Bill S-30; and R. Humphreys, Superintendent of Insurance.

The Chairman presented the Seventh Report of the Sub-Committee on Agenda and Procedure, dated December 7, 1966, which is as follows:

Your sub-Committee on Agenda and Procedure met at 1:00 p.m. this day and has agreed to recommend as follows:

- (a) That briefs from the undermentioned, received after the deadline of November 1st, be accepted by the Committee:

Prof. E. P. Neufeld, University of Toronto  
Canadian Federation of Agriculture  
A group of Twelve Trust Companies

- (b) That briefs received from the undermentioned, who have indicated they do not wish to appear, be circulated forthwith to the members and published in the final issue of the Minutes of Proceedings and Evidence on the banking legislation:

S. A. Bensh, Nanaimo, B.C.  
Canadian Chamber of Commerce  
Lloyd H. Denning, A.P.A., Dunnville, Ontario  
James M. Dever, Montreal  
H. Latulippe, M.P.  
Alex Mills, C.L.U., Toronto  
A. M. Moore, Dalhousie University

- (c) That the following be invited to appear before the Chirstmas recess:

H. H. Binhammer, Royal Military College, Kingston  
R. Caterina, Carleton University  
Canadian Credit Men's Association, Ltd., Toronto  
E. P. Neufeld, University of Toronto  
David W. Slater, Queen's University  
Jacob S. Ziegel, McGill University

- (d) That the Chief of the Committees and Private Legislation Branch be authorized to engage the services of reference index personnel for the purpose of indexing Proceedings on the banking legislation now before the Committee when it is printed in "blue book" form;
- (e) That on Thursday, December 8th, the Committee consider Bill S-30, An Act to incorporate League Savings and Mortgage Company.

On motion of Mr. Wahn, seconded by Mr. Fulton, the report was *approved*.

The Chairman stated that pending approval by the Committee tentative arrangements had been made for the following to appear on the dates mentioned:

Professors Binhammer and Slater on Tuesday, December 13th

Professors Neufeld and Ziegel on Thursday, December 15th

Professor Caterina and representatives of the Canadian Credit Men's Association Limited on Tuesday, December 20th.

The Committee then proceeded to consideration of Bill S-30, An Act to incorporate League Savings and Mortgage Company.

#### *On the preamble*

Mr. MacEwan, sponsor of the Bill, introduced the Parliamentary Agent, Mr. Blair, who explained the purpose of the Bill. Mr. MacMullin also made a brief statement.

Mr. Humphrys stated that the proposed company has met the requirements of his Department.

Messrs. MacMullin, Blair and Humphrys were questioned and the preamble was carried.

Clauses 1 to 7 inclusive and the Title were severally carried.

The Bill was carried without amendment.

*Ordered*,—That the Chairman report the Bill without amendment.

Reverting to the Banking legislation now before the Committee, the Chairman tabled the following papers provided by the research assistants in answer to questions raised by members:

The Regulation of Foreign Banks in the United States, by Professor Jack Zwick, Columbia University,

A study of foreign banking operations in the United States prepared by Professor Zwick for the Joint Economic Committee of the United States, Bank of Canada Statistical Summary, November 1966.

*Ordered*,—That the papers listed above be distributed to the members and that the Bank of Canada Statistical Summary be distributed monthly.

At 12:10 p.m. the Committee adjourned until Tuesday, December 13th at 11:00 a.m.

Dorothy F. Ballantine,  
*Clerk of the Committee.*



## EVIDENCE

(Recorded by Electronic Apparatus)

THURSDAY, December 8, 1966.

The CHAIRMAN: Gentlement, I see a quorum.

The legislation on our agenda this morning is Bill No. S-30, An Act to incorporate League Savings and Mortgage Company.

First, I would bring to your attention the report of the Steering Committee, arising out of its meeting of yesterday, which reads: (*See Minutes of Proceedings*)

I ask for a formal motion to approve this report.

Mr. WAHN: I so move.

Mr. FULTON: I second the motion.

The CHAIRMAN: Anticipating approval of the steering committee report, I asked the clerk to make some enquiries, and she has handed me this note saying that Drs. Binhammer and Slater can appear on Tuesday, December 13th; that Drs. Neufeld and Ziegal can appear on Thursday, December 15th; that Dr. Caterina and the Canadian Credit Men's Association, Limited, can appear on Tuesday, December 20th, assuming, of course, that the House will be meeting at that time.

I have also suggested to the Steering Committee that as soon as we know a little more definitely when we will adjourn and when we will resume after Christmas, we call a meeting immediately to plan our program for the resumed session in the new year.

Is there any comment on the motion before us?

Motion agreed to.

The CHAIRMAN: To proceed to our order of business, we have with us Mr. MacEwan, the sponsor of Bill No. S-30 and, before asking him to introduce formally those who are supporting the bill, I should indicate they are Mr. D. Gordon Blair, the Parliamentary Agent, and Mr. R. D. McMullin, Managing Director of the Nova Scotia Credit Union League. Also in attendance is Mr. R. Humphrys, Superintendent of Insurance.

Mr. MacEwan, I hope I have not stolen your thunder in mentioning this, but I know you have a word, as sponsor, with respect to the people who are with us and the bill that we are going to consider.

Mr. MACEWAN: Mr. Chairman, you have introduced the gentlemen here with me today who will answer the necessary questions.

I am appearing as sponsor of the bill and not as parliamentary agent or counsel.

I set out in the House of Commons, on second reading, the objects of setting up League Savings and Mortgage Company, which will be a subsidiary of the Nova Scotia Credit Union League.

May I just say succinctly that this company is necessary and will be of great benefit, if this act is passed together with the Credit Union League and the various credit unions in the province of Nova Scotia, in providing the necessary mortgage funds to many areas of our province where the ordinary commercial companies do not provide funds at the present time.

Thank you, Mr. Chairman.

The CHAIRMAN: Thank you very much, Mr. MacEwan. We all know the role played by the people of Nova Scotia in developing the credit union and cooperative movement.

I will now call upon the parliamentary agent to make any introductory comments he may have, in association with Mr. McMullin. Then I will ask the Superintendent for any comments he may have.

Mr. D. Gordon BLAIR (*Parliamentary Agent*): Mr. Chairman and gentlemen, I can add nothing to the excellent presentation of the measure made by Mr. MacEwan in the House.

Mr. Howard, in the course of the House of Commons debate, raised an important question. He wanted to be sure that control of this company would never get away from the credit union movement, and I believe that Mr. McMullin, in the course of the few remarks he might make, will be able to deal with this question. Mr. McMullin?

Mr. R. D. McMULLIN (*Managing Director, Nova Scotia Credit Union League*): Mr. Chairman and gentlemen, there is no great need for me to go into any background on the bill. Mr. MacEwan has given a very excellent introduction to it in the House, and I think he has covered it pretty much in detail as far as background is concerned.

I want just to emphasize again that the real purpose of this bill is to enable the League, as the central organized body of the credit unions in Nova Scotia, to make available in greater measure a mortgage lending service to our members. This is in process largely because of the fact that there are many areas in our province where the conventional mortgage services are not available, either because of low real estate values, fund conditions, or for other reasons, with the result that, over the years, credit unions and particularly the League have been called upon to provide a limited service in this particular field.

It is in recognition of the very limited resources that we have, and the limited service that we can give, under present circumstances, that we are asking for incorporation of League Savings and Mortgage Company so that we can expand and extend what we are now doing in this particular field.

Mr. Howard raised a very interesting question a few days ago when this bill was presented to the House. It is one that we certainly appreciate very much as credit union members and as co-operators, because it is a basic co-operative principle that in co-operative organizations individuals vote, and not money, so that it has been traditional for one member to have one and it has also been traditional, in the case of federations, that the vote be a delegated vote whereby a corporation federated into another body, such as the credit unions into the League, work in a delegate system.

So far as this new company is concerned, we recognize that this is a private company where the voting will be done on the basis of share capital in exactly the same way as any other private company. However, in recognizing this, we also recognized that we still wanted to maintain control of the company within the movement, so far as this is humanly and legally possible. Therefore, it would be the intention of the credit union movement in Nova Scotia that this company would be operated as a subsidiary of the League, with the bulk of the shares being held by the League itself; and that all the credit unions that are now members of the League would also hold shares in the organization, but probably to a lesser extent.

The annual meeting of this new company would be held at the same time and place as the annual meeting of the Nova Scotia Credit Union League.

We anticipate that the delegates who would be carrying the votes of the various credit union shareholders of this new organization would be the same people who would be the delegates representing their respective credit at the annual League convention. Therefore, for all practical purposes, the delegates who will be voting on this new company, provided it is incorporated, will be exactly the same people as those who attend the annual meeting of the League, which is actually the policy-making body of the credit union movement in the province. These are going to be exactly the same people, meetings will be held at the same time, so there will be every opportunity for the League and the credit unions to retain control of this organization as we have anticipated.

So far as it is possible to write this into legislation, we will be attempting to do so—certainly by bylaw—and we are told by legal counsel that it is at least possible to restrict the transfer of shares so that they cannot be transferred effectively to anyone outside the credit union movement.

This is the situation as we visualize it, and I feel quite confident that the provisions we have in mind that will be incorporated into bylaws, as well as into convention policy, will ensure that control of the new company will always remain within the credit union movement, I believe that this will answer, to a large extent, the very important question that was raised by Mr. Howard when his was presented in the House a few days ago.

The CHAIRMAN: Thank you, Mr. McMullin. It is to be understood, of course, that the preamble has been taken as called, and strictly speaking this discussion is taking place on the preamble.

Mr. Humphrys, do you have any comments to make on this application?

Mr. R. HUMPHRYS (*Superintendent, Department of Insurance*): Mr. Chairman and gentlemen, Mr. McMullin, on behalf of the League, has discussed the proposed company with the Department. We are aware of their plans, and we have no objection to the formation of the company. Although we do not supervise the Nova Scotia Credit Union League, which is the central credit union for the Province, we have become very well acquainted with it over the years. Our feeling is that its function as a central credit union for the local credit unions is probably better served if the mortgage lending is done in a separate corporation, rather than in the League. We believe that this is a good development for the movement in Nova Scotia.

The bill is in standard form. It will be a loan company under the Loan Companies Act and subject to the Loan Companies Act in all respects.



The CHAIRMAN: I presume that while you do not supervise the credit union group you will, under the law, be supervising the loan company which we are considering today?

Mr. HUMPHRYS: Yes, Mr. Chairman.

The CHAIRMAN: They have met all your requirements to date?

Mr. HUMPHRYS: That is correct, sir.

The CHAIRMAN: We are now open for questioning of any of our witnesses. I recognize first Mr. Lambert, followed by Dr. McLean.

Mr. LAMBERT: Mr. Chairman, I regret that I did not hear Mr. MacEwan's exposition as sponsor of the bill, and I am intrigued a little by the rationale, or the motivation, of coming for a federal charter for a credit union movement that is limited to the province of Nova Scotia. I was wondering whether the reason is that there is no appropriate legislation in the province of Nova Scotia which would meet the objectives that have been indicated by counsel and by Mr. McMullin and, no doubt, by Mr. MacEwan.

Mr. McMULLIN: There are probably two answers to this question. First of all, our solicitors recommended that we seek federal incorporation—and the reason probably was more appropriate for 1966 than any other year—because there was, in the minds of the Canadian public, a certain distaste resulting from some of the happenings in the financial field during the last couple of years, of which you are aware. Therefore, we were advised, from the point of view of developing and maintaining public confidence, that it would be preferable to have a federal incorporation rather than a provincial incorporation, because although the latter may be more easily obtained and would, for all practical purposes, give us practically the same legislation, it was felt that federal incorporation, with the assurance of federal supervision, would increase public confidence in the organization.

The second reason—probably not an important one—is that for a number of years there has been consideration in the maritime area of maritime union as far as cooperative development and credit union development are concerned. In anticipation that this might come about at some time it was considered that federal incorporation would be preferable, because if we did develop the maritime credit union league setup it would, enable us to operate in the other two maritime provinces. However, at the moment there is no intention of going outside Nova Scotia with the company.

Mr. HUMPHRYS: Mr. Chairman, could I add a comment? There is another factor that may be relevant.

For many years the federal Department of Insurance has supervised trust companies, loan companies and insurance companies in Nova Scotia. They have had the federal superintendent do the supervising work for their institution, and to that extent, if we are going to supervise the company, there are certain advantages in having it under the legislation that we administer rather than supervising it in terms of other statutes under which we have no rights.

The CHAIRMAN: You do this by agreement?

Mr. HUMPHRYS: Yes.

Mr. LAMBERT: A sort of subcontract.

Is it the intention of the proposed company to accept deposits from the public as a source of its funds, or will the funds be provided strictly out of the capital provided through the federation of credit unions?

Mr. McMULLIN: We anticipate that all the share capital will come from the credit unions and the League, and that the rest of the resources that the new organization will have for the purpose of making mortgage loans will come largely from the sale of debentures. These debentures will be sold to our credit unions and to the general public; so that, for the most part, the actual money that will be used for making mortgage loans will come from the sale of debentures to the general public.

We have not given any particular thought to the idea of accepting deposits, although this is possible under the bill as the organization develops, with the approval, I believe, of the Superintendent of Insurance. We have not at the moment given any thought to the idea of accepting deposits, although this is a possibility in the future.

Mr. LAMBERT: The reason I am interested is that in what is reported to be the legislation which may cover deposit insurance, the fact that this company would have a federal charter would likely preclude it from getting the consent of the province. I was wondering whether this was, perhaps, one of the motivations in coming before Parliament to get a federal charter.

Mr. McMULLIN: No, we had not given this too much consideration as a reason for coming for federal incorporation, although we are conscious of the possibilities of federal deposit insurance.

The other thought that we do have in our minds, though—and which makes us just a little bit hesitant to say “yes” or “no” to your question at this time—is the possibility that there might be some objection from our credit union people generally if we accept deposits, because this could possibly be considered as competing with the credit unions for deposit money, and we would not want this to happen.

Mr. LAMBERT: It seems to me that one of the motivations for the establishment and expansion of the original credit union movement was to get away from the activities of loan companies, and here we are coming, shall we say, full circle, with the league of credit unions coming back to found its own loan company.

Mr. McMULLIN: Yes; I doubt that we would be too anxious to get into the deposit field because we would prefer, at the moment anyway, to have the credit unions act as the primary depositories for funds, and any surplus funds they have could be invested in this new company by way of debentures.

Mr. LAMBERT: I have a couple more questions, Mr. Chairman. Under clause 4 of the bill, have you yet had a subscription for \$500,000, and when do you anticipate that you could call your first meeting of the shareholders?

Mr. McMULLIN: This can be done almost any time after the company has been approved by Parliament, and the proper time for making the subscription has been determined.

Mr. LAMBERT: Have you any binding agreements with the League, or with any of its members, that they shall subscribe?

Mr. McMULLIN: All of the necessary authority in this respect has already been given as far as the League itself is concerned, and as the credit unions have unanimously approved at convention the idea of the company I anticipate no problem in having them subscribe a portion of the funds.

Mr. LAMBERT: There is a good portion of Nova Scotia where the French language is used extensively, and within the credit union movement. If it is anticipated that this will expand into a maritime operation, I am wondering why you did not apply at this time for the French version of the name. Or is it your intention to proceed, under the new section 6 (a) of the Act, to the Governor in Council for a French version?

Mr. McMULLIN: This has actually been considered, and I have no explanation of why this has not been done. We would be happy to include the name now, if it is appropriate. It has been assumed, I believe, that this could automatically be used.

Mr. LAMBERT: I would not insist on it. I was merely wondering why it was not done here, because otherwise it has to go back to the Senate with the amendment. There is provision in sections 64 and 65 of the new Act for direct application through Mr. Humphrys to the Governor in Council for this, but a matter of public relations I wondered why it was not included.

Mr. BLAIR: I think, Mr. Lambert, the point you have made is well taken. To avoid the complications of trying to prepare an adequate translation of the name here, probably it would be preferable to proceed under the special authority which now exists.

The CHAIRMAN: I gather that you are making it clear, gentlemen, that you have no objections to doing this, and that you are prepared to take this step?

Mr. LAMBERT: I am rather amazed at what I think is a lapse in public relations, if I may say so.

The CHAIRMAN: They might want to be the first ones to use the provisional new law.

Mr. LAMBERT: No, I think it would be better on the incorporating of the bill, but I will leave it at that.

Mr. McMULLIN: It is included in our credit union legislation, but we did not think of it for this.

Mr. LAMBERT: That is all, Mr. Chairman, thank you.

The CHAIRMAN: Dr. McLean?

Mr. McLEAN (*Charlotte*): Mr. Chairman, most of my questions have been answered already.

I understand that your debentures are going to be sold to the general public and not confined to the credit unions, but that your shares are going to be confined to the credit unions. Therefore, the general public will have no say about anything that happens about the debentures. They will not be represented.

Mr. McMULLIN: That is right.

Mr. McLEAN (*Charlotte*): All my other questions have been answered.



The CHAIRMAN: With regard to Dr. McLean's point, is this situation on the debentures any different from those sold by any other savings and loan organization? Are you aware of any provisions for representation by debenture holders?

Mr. BLAIR: It is no different.

The CHAIRMAN: Are there any other questions from members of the Committee? Mr. Cameron, followed by Mr. Fulton and Mr. Gilbert.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Is it the intention to set up branches in various centres in Nova Scotia, or are you going to operate through these credit unions?

Mr. McMULLIN: We have not given any thought at this stage to setting up branches. It is possible that at some future time we will have a branch in the Sydney area, which would cover the Cape Breton area, and possibly a couple of the other large areas. At the present time we have a branch operation of our present organization in Halifax. Our head office is in Antigonish, and we have a field staff represented in the Cape Breton area. It is very likely that with the head office of this new company in Halifax we will at least have a branch office in the Cape Breton area in the foreseeable future, although at the moment there is no thought being given to this.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Can you tell me how a person living at some distance from either Antigonish or Halifax would go about applying for a loan?

Mr. McMULLIN: That is a very good question, and I am glad you have brought it up, because in processing mortgage loan applications I believe that the reason for the exceptionally fine success we have with it at the present time and have had for the past number of years, is the fact that all applications that we have coming to us for mortgage loans come by way of our local credit union. In other words, the applications that we take care of are already recommended to us by the credit committee of the applicant's credit union. The application goes first to the individual's credit union, and from there it is sent to the League with a recommendation that it be granted. In this way we have a fair amount of participation and responsibility on the part of the local group as well as at the League level. We would anticipate this same kind of arrangement with the new company.

The CHAIRMAN: This means that someone from Windson, Nova Scotia, would have equal access to the facilities?

Mr. McMULLIN: That is right.

The CHAIRMAN: The credit union branches would, in effect, be agents in this regard?

Mr. McMULLIN: Yes. They are not legal agents, as such, but they would certainly be used to transfer applications to us, and would be used to screen applicants.

The CHAIRMAN: So the voluntary work of the credit committee would help to reduce the overhead cost of your operation?

Mr. McMULLIN: Yes; I think this is one of the reasons why, up to this point, we have been able to make mortgage loans successfully from the League in areas that would not normally be classified as good areas for investment by the conventional mortgage companies.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I take it that the credit unions will hold the majority stock in the company?

Mr. McMULLIN: Yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Thank you. That is all I have.

The CHAIRMAN: I now recognize Mr. Fulton, followed by Mr. Gilbert.

Mr. FULTON: Mr. Chairman, could I ask whether the arrangements by which it is intended that the control will reside in the credit unions will be by putting in the bylaws a restriction on the right to transfer shares?

Mr. McMULLIN: I do not know whether in the bylaws, we can restrict the actual sale of shares, although we would certainly do this as a matter of policy. I anticipate that the delegates from the credit unions would want to do this, and I cannot see it otherwise. I am not sure that this can be done legally in the bylaws.

Perhaps Mr. Humphrys or Mr. Blair could answer this.

Mr. FULTON: It is not exactly a private company, and I am wondering whether you can, therefore, put the kind of restriction that you normally find in private companies.

Mr. BLAIR: Mr. Fulton, I believe the preliminary view is that it may be possible to make the actual transfer of the shares on the books of the company subject to the approval of the directors, but if that is found to be impossible then a shareholders' agreement will be created which will bind all the shareholders of the company.

Mr. FULTON: Therefore, your right would be only to proceed against the shareholder. You would not have the power to hold up a transfer of shares, *ab initio*. You would have to seek an order of the court compelling him to retransfer, or to nullify any transfers made outside the terms of the agreement?

Mr. BLAIR: That would be the legal way in which it would have to be carried into effect; but, of course, the real sanction would be the determination of the credit unions, as expressed at their meetings and conventions, to hold this company in their hands.

Mr. FULTON: Have draft bylaws been prepared?

Mr. McMULLIN: They are being worked on now, but they have not been developed because we wanted to be sure that the company was going to be incorporated before we got into this.

The CHAIRMAN: But you are also considering the concept of an agreement with the shareholders of the League itself?

Mr. BLAIR: Yes.

Mr. McMULLIN: We are certainly very conscious of this, and we would do everything possible to make sure that the shares of the company will always be

retained by the League and by credit unions that are affiliated with the League. So that if a credit union did want to dispose of any shares which it had I would think that the League would want to buy up such shares immediately. For instance, if a small credit union should be going out of existence, as does happen these days with amalgamations of the smaller ones, we would anticipate that any such shares would be bought up by the League itself, rather than transferred outside. This could be done by agreement, I am told.

Mr. FULTON: I may be raising a point that is not very likely to occur, but if the restriction on the right to transfer shares is not covered in the articles or bylaws of the company, what is the position of a bona fide purchaser for value, if it is only covered in some agreement of which he has no notice? In other words, what is the position if somebody forgetfully, or deliberately, sells his share to a bona fide purchaser for value?

Mr. BLAIR: I would think that the bylaws would give notice of this provision or, if it had to be done by shareholders agreement—and I am not persuaded that they would have to do it that way—the bylaws at least could give notice of the existence of such an agreement.

Mr. FULTON: Mr. Humphrys, do you know off-hand whether a loan company incorporated under this act can, in fact, put restrictions in its bylaws on the right to transfer shares.

Mr. HUMPHRYS: I cannot give you a positive answer, Mr. Fulton. We have not had advice from the Department of Justice on that particular point. My own feeling, for what it is worth, would coincide with Mr. Blair's.

Mr. McLEAN (*Charlotte*): May I ask a supplementary question? I happen to belong to a company where the shares must be offered to other members of the company before they can be sold to the public.

Mr. FULTON: Is that a private company?

Mr. McLEAN (*Charlotte*): No, it is incorporated.

Mr. FULTON: Yes; but is it a private company?

Mr. McLEAN (*Charlotte*): You might say that it is a closed corporation.

The CHAIRMAN: Mr. Lambert, do you have a supplementary question?

Mr. LAMBERT: Surely if there are these shareholders' agreements the bylaws will have to provide authority to the directors to enter into such agreements, because they are not the type of powers that are normally given to directors for the administration of a company. As Mr. Fulton has indicated, my own views are that it would be preferable to have these right within the bylaws rather than have shareholders agreements, because if there is no power to the directors to enter into such agreements then any such agreement is *ultra vires*.

The CHAIRMAN: Gentlemen, you have just seen a further advantage of federal incorporation in that by coming before this Committee, in addition to the assistance of your very capable counsel, Mr. Blair and the Nova Scotia counsel, you are getting free legal advice from two of the most high-powered counsel in Canada.

Mr. FULTON: Probably it is worth as much as they are being charged for it.



The CHAIRMAN: No, I would put it much higher than that. I just mention it as another benefit of federal incorporation which has not been recognized until now, that in addition, you get advice from some very senior people who have studied the business field, sometimes very critically.

Have you any further questions, Mr. Fulton?

Mr. FULTON: No.

The CHAIRMAN: I now recognize Mr. Gilbert.

Mr. GILBERT: Mr. Chairman, I wonder if Mr. McMullin would tell us whether their mortgage loans will be restricted to credit union members?

Mr. McMULLIN: I would think so, yes.

Mr. GILBERT: And not to the public at large?

Mr. McMULLIN: I would think that they would be restricted, if not in legal terms, certainly in actual practice, to credit union members.

Mr. GILBERT: But you are not required to restrict your loans to credit union members?

Mr. McMULLIN: No.

Mr. GILBERT: You say that the credit union league has made mortgage loans to credit union members in the past. What is the pattern of that mortgage? Does it contain a penalty clause with regard to repayment?

Mr. McMULLIN: There is no penalty clause. As a matter of fact, our situation has been such that we welcome prepayments because we always have a much greater demand for loans than we have resources. If someone wants to prepay his mortgage we are very happy about it because we are able to reinvest this in another loan and satisfy another person who is waiting.

Mr. GILBERT: What has been your range of mortgage interest rates?

Mr. McMULLIN: At the present time our interest rates are 8 per cent. These include the popularly known loan protection insurance program which actually costs us about three-quarters of one per cent; so that, comparatively speaking, our rate is about  $7\frac{1}{4}$  per cent.

Mr. GILBERT: Is there any provision for rebates? In an ordinary credit union if you take out a loan a rebate is given at the end of the year.

Mr. McMULLIN: Right now it is not done by way of a rebate to the borrowers. We feel that the borrowers are getting a rebate by virtue of the fact that traditionally we have charged a much lower rate for our mortgage loans than do the conventional companies. All of the earnings of the League on mortgages and so on have been going back to the credit unions as interest on their deposits or their capital investment with the League. We have not, as a rule, rebated to the individual borrowers.

Mr. GILBERT: I think that is all, Mr. Chairman.

The CHAIRMAN: I have a question.

As you gentlemen know, we are considering draft legislation which would empower banks to take mortgages quite freely. Have you assessed the possible impact of this on your own plans.

Mr. McMULLIN: No. I think this would be an advantage, too, to our people if the banks were making mortgage loans, because as it is right now we have a large number of people who are unable to get mortgages, and, in many cases, where they do get mortgages they get them at an extremely high rate of interest. As a matter of fact, I saw one negotiated just a few days ago at 14 per cent, which is an extremely high rate of interest.

We would certainly be happy if the banks were able to grant this individual a mortgage even at half this rate.

Mr. MONTEITH: Mr. Chairman, may I interject a supplementary? Would the actual field to be covered by the proposed loan company really be that which the banks would ordinarily cover? You have a sort of field in which it is difficult to get coverage right now, have you not?

Mr. McMULLIN: This is true; although we have to recognize the fact, too, that among our 90,000 credit union members in Nova Scotia today we do have very nearly all segments of society covered. We find that we have a lot of what you might call "white collar workers"—middle class people—borrowing from credit unions because of preference. They could get it elsewhere, probably, but they prefer to get it from the credit union because they are associated with the credit union as government employees, or as people in industry, or whatever it might be.

Sometimes it is because there is less red tape; sometimes they feel that they would get better treatment from their credit union; and some people place a lot of value in the automatic loan protection insurance that is made available at no extra cost. These individual choices are the reasons why people in almost any bracket of society may prefer to borrow from a credit union or from a credit union league rather than from outside sources.

The CHAIRMAN: I think Mr. Monteith's question really was aiming at the point I was interested in, and that is whether or not the new powers that are proposed for the banks in the mortgage field would reduce the impact of what you want to do.

Mr. McMULLIN: I do not think so. We have the banks operating in the consumer loan field and it really has not affected the growth of credit unions. I cannot imagine that if the banks get into the mortgage lending field that this is going to have much effect. In my part of the country we have such a backlog of mortgage applications to be filled that I would think there is room for a long time to come for almost any legitimate organization to enter this field and offer this service.

It is possible that we will be operating in some areas where banks and other conventional companies may not prefer to invest too heavily, but I think we can do this safely by virtue of the fact that we are better able to assess character and other factors to our advantage better than can other lending companies.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I think, Mr. McMullin, that it should be made quite clear that the banks, although they are given a federal charter, have no God-given right to have a monopoly in this field. If the people of Nova Scotia want to embark on it themselves they have every right to do so.

The CHAIRMAN: That is quite so, Mr. Cameron, and the reason that I pose this question is to see whether the witness would be willing to state quite clearly that his organization would continue to play a very needed and useful role, even though we are considering other legislation.

Mr. McMULLIN: Oh, yes; this would not interfere with us at all.

The CHAIRMAN: You would still have a very useful and important role to fill that would not be otherwise disposed of?

Mr. McMULLIN: Yes.

The CHAIRMAN: I recognize Mr. Gilbert on a supplementary, and then Mr. Flemming.

Mr. GILBERT: Mr. McMullin, is the League Savings and Mortgage Company restricted to giving first mortgages, or can they also give small second mortgages?

Mr. McMULLIN: No; it would be restricted to first mortgages.

Mr. HUMPHRYS: The corporate power is not so restricted.

Mr. GILBERT: I see. In other words, they would have power to give small second mortgages?

Mr. McMULLIN: I think we would automatically restrict it to first mortgages. If second mortgage financing were necessary we would hope that we could work out some sort of arrangement with the local credit union to assist on this.

Mr. GILBERT: What about the type of construction? Is it intended to finance old homes as well as new homes?

Mr. McMULLIN: We hope that we will continue in much the same way as we are now, which is making money available for new construction, for the purchase of existing homes, and for the major renovation of existing homes.

Mr. GILBERT: That is all, Mr. Chairman.

The CHAIRMAN: Mr. Flemming, and then Mr. Lambert has some further points he wants to raise, I believe.

Mr. FLEMMING: Mr. McMullin, you mentioned that you might extend your activities into adjoining provinces and I presume the credit unions making up your League are located entirely in Nova Scotia at the moment?

Mr. McMULLIN: Yes.

Mr. FLEMMING: If you did enlarge your scope and take in New Brunswick, for instance, would it be your intention also to take into the League any credit unions located in New Brunswick?

Mr. McMULLIN: As you know, the credit union movement in the Maritimes has always worked very closely together, so that we have always worked very closely with the Brunswick Credit Union Federation and the Federation de Caisse Populaire Acadien, Caraquet, as well as in Prince Edward Island. From time to time consideration has been given to the idea of developing a maritime credit union movement with one central credit union organization and one central co-operative organization and so on. Nothing has actually developed on this, but if this eventually does come about, this new company would have



automatically, by virtue of its federal incorporation, the powers to go into New Brunswick and Prince Edward Island and provide its services there, subject, of course, to the invitation to go in there coming from the credit union people in New Brunswick and the credit union people of Prince Edward Island.

Mr. FLEMMING: In any event, I take it that you have authority, and you have taken some preliminary steps so far as discussion is concerned, and you think that perhaps one of the advantages of this bill might be that it would give you definite authority to do this very thing if everyone concerned were desirous of doing it. Is that right?

Mr. McMULLIN: That is right.

The CHAIRMAN: Thank you, Mr. Flemming.

(Translation)

I now give the floor to Mr. Latulippe because his name is next on my list. Will you put your questions?

Mr. LATULIPPE: Yes, thank you, Mr. Chairman. Mr. Flemming has just put the question I intended to put with regards to the advantages that will accrue to the Corporation by benefitting from conducting transactions conducted in the other provinces. I think it was mainly because you want to conduct business in other provinces, that you want a federal charter, is that not right? You will be able to conduct business in the other provinces if you have a federal charter, that is the main reason for which you are asking a federal charter, is it not?

(English)

Mr. McMULLIN: Yes. It is not the main reason, but it is a consideration in our asking for federal incorporation, so that eventually, if it is desirable to operate in the other provinces and especially in the maritime provinces, we would have the powers to do so.

(Translation)

Mr. LATULIPPE: Will your corporation be going into all fields of the economy? Will you be lending in various areas: in industry, residential homes, mining? Will you be going into all these fields?

(English)

Mr. McMULLIN: We expect to go into the fields of residential mortgage loans, primarily. We would make no distinction whether or not these were in urban areas, or in rural areas with our farmers and fishermen.

As a matter of fact, at the present time, we have a substantial amount of our mortgages invested in rural areas, to farmers and to fishermen. We do not anticipate getting into commercial loans, as such, as we would expect that our commercial loans to co-operatives, to farm organizations, and so on, would be carried on as they are now through a department of the credit union league itself.

Our League is made up of three departments, one of which is our deposit and loan department, and it is through this department that we make loans to credit unions, to cooperatives and to organizations of this nature, and we would

continue to do this; so that commercial loans would be made by the league, with the residential loans being made through the new company.

(Translation)

Mr. LATULIPPE: Will the stockholders in your corporation be limited?

(English)

Mr. McMULLIN: The stockholders will be limited to the credit union league itself, as one, and the other credit unions located in the province that are members of the League. At the present time, all of the credit unions in Nova Scotia, with one exception, are members of the League, and we anticipate that this credit union will be coming into the fold very shortly. Therefore, it would be limited to these organizations and the League.

At the present time, we have roughly 170 credit unions in Nova Scotia so that we can anticipate that if there is no change there will be roughly 171 shareholders of the new company.

(Translation)

Mr. LATULIPPE: In conclusion, you can count on our group helping you. We certainly could not oppose this, we will approve your request, we are happy to approve it.

The CHAIRMAN: Thank you, Mr. Latulippe. Now, Mr. Comtois.

Mr. COMTOIS: Is it a fact that you intend to operate in several provinces. Have you thought of choosing a French name for your new corporation? What would be the translation?

The CHAIRMAN: Mr. Comtois we have already put this question. I can help you in this important matter. The group has already told us that they are quite ready to have a French name and they intend to use the new powers under the Canadian Corporation Act. They intend to make an application to the Governor-in-Council for a French name for their company. That was the reply they gave us earlier.

(English)

Mr. LAMBERT: I believe Mr. McMullin told us that it was the intention that all the share capital should be held by the league or credit unions with the exception, of course, of the qualifying shares for directors under section 18. This would create a different class of shareholder, because there cannot be any declaration of trust or anything of that nature. They must be bona fide owned by all of the directors. That is understood?

Mr. McMULLIN: Yes, that is right; the corporation—

Mr. LAMBERT: As a matter of fact the shares could not be owned by the credit union and the nominee act as a director, because the new section 18, which I believe, is in much the same terms as the old section is pretty clear in that regard.

I think you might have a little problem here about the holding of your shares.

Mr. BLAIR: I think the answer, Mr. Lambert, is that in practice this is, in effect, a family corporation, and had the credit union league had any real concern about its ability to handle these rather technical problems then it would have sought an enlargement of the powers in the model bill. But these really are matters of no consequence operationally, because it can be assumed that no difficulty is going to arise in practice.

Mr. LAMBERT: I was concerned about the statement that the "shareholdings would be by the League or its members" when, in essence, the Loan Companies Act forbids this.

Mr. BLAIR: Yes, as far as the directors are concerned.

Mr. LAMBERT: Yes, as far as the directors are concerned.

The CHAIRMAN: I gather that there are no further questions or comments.

Preamble agreed to.

Clauses 1 to 7 inclusive agreed to.

Title agreed to.

The CHAIRMAN: Shall I report the bill without amendment.

Some hon. MEMBERS: Agreed.

The CHAIRMAN: Gentlemen, we are ready to adjourn, and I want to thank the witnesses today for giving us an opportunity to consider this bill which will be of great assistance to the credit movement initially in Nova Scotia and, perhaps, later on, through the maritimes and the rest of our country.

I have asked our research staff to make sure that every member of the Committee has available the monthly bulletins of the Bank of Canada until we complete our study of the banking legislation. Some members have it already but it comes out monthly.

I have also procured copies of the Zwick memoranda which were provided to the Joint Economic Committee of the United States Congress, another version of which appeared in a banking journal in the United States.

If it is the wish of the Committee I will instruct our clerk to have this material circulated. It might help us in some of the things we are going to be getting into. I am not suggesting, by the way, that this be printed; I want to make this very clear. It is not that there is anything wrong with printing it, but the material is rather bulky and there might be problems in some cases in getting permission, and so on; but if it is the wish of the Committee I will have this material circulated.

Our next meeting will be on Tuesday, December 13, at which time our witnesses will be Dr. Binhammer of Royal Military College, and Dr. Slater of Queen's and, of course, the necessary background material will be circulated.

Mr. McMULLIN: I would like to say a very hearty "thank you" to you people who have given up your time to consider this bill, especially to Mr. MacEwan who introduced it, and others of the Committee and in the House who have spoken on it and who have raised very important questions. We appreciate all of these. We can assure you that we will do everything that we possibly can, through our bylaws and through the provisions of the act, to conform to the best traditions of the co-operative movement, and we hope that the operations of this



new company will justify the time, effort and confidence that you have placed in us. Thank you very much.

Mr. MACEWAN: May I just endorse that, and thank the members of the Committee and say, as a member of the legal profession who acts once in a while, that this has served as a refresher course in corporate law.

The CHAIRMAN: You might also express a form of thanks to Mr. MacFadden of the Mercantile Bank, in a sense, as he felt that he needed a further period to recover from his pleurisy and, therefore, we were able to hear you earlier in our schedule than otherwise would have been the case.

The meeting is adjourned.



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LÉON-J. RAYMOND,  
*The Clerk of the House.*



HOUSE OF COMMONS  
First Session—Twenty-seventh Parliament  
1966

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STANDING COMMITTEE

ON

FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. HERB GRAY

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MINUTES OF PROCEEDINGS AND EVIDENCE

No. 31

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TUESDAY, DECEMBER 13, 1966

Respecting

Bill C-190, An Act to amend the Bank of Canada Act.

Bill C-222, An Act respecting Banks and Banking.

Bill C-223, An Act respecting Savings Banks in the Province of Quebec.

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WITNESSES:

H. H. Binhammer, Associate Professor of Political and Economic Science,  
Royal Military College; David W. Salter, Professor of Economics,  
Queen's University.

ROGER DUHAMEL, F.R.S.C.  
QUEEN'S PRINTER AND CONTROLLER OF STATIONERY  
OTTAWA, 1966

STANDING COMMITTEE  
ON  
FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. Herb Gray

*Vice-Chairman:* Mr. Ovide Laflamme  
and Messrs.

Addison,	Comtois,	Leboe,
Basford,	Flemming,	Lind,
Cameron ( <i>Nanaimo-</i>	Fulton,	McLean ( <i>Charlotte</i> ),
<i>Cowichan-The Islands</i> ),	Gilbert,	Monteith,
Cashin,	Irvine,	More ( <i>Regina City</i> ),
Chrétien,	Lambert,	Munro,
Clermont,	Lamontagne,	Valade,
Coates,	Latulippe,	Wahn—(25).

Dorothy F. Ballantine,  
*Clerk of the Committee.*

## MINUTES OF PROCEEDINGS

TUESDAY, December 13, 1966.  
(60)

The Standing Committee on Finance, Trade and Economic Affairs met at 11:10 a.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Addison, Cameron (*Nanaimo-Cowichan-The Islands*), Clermont, Flemming, Gilbert, Gray, Laflamme, Lambert, Lind, McLean (*Charlotte*), Monteith, Wahn—(12).

*Also present:* Messrs. Grégoire and Johnston.

*In attendance:* Messrs. H. H. Binhammer, Associate Professor of Political and Economic Science, Royal Military College; C. F. Elderkin, Inspector General of Banks; and Miss M. R. Prentis, research assistant.

The Committee resumed consideration of the banking legislation.

The Chairman introduced the witness, Mr. Binhammer, who made an opening statement, copies of which were distributed to the members. In accordance with the resolution passed at the meeting of October 13, 1966, Mr. Binhammer's brief is attached (*See Appendix W*).

The witness was questioned.

At 11:40 a.m. the Vice-Chairman took the Chair, and at 11:50 a.m., the Chairman resumed the Chair.

The questioning having been concluded, the Chairman thanked the witness, who was permitted to retire.

At 1:05 p.m., the Committee adjourned until 3:45 p.m. this day.

### AFTERNOON SITTING (61)

The Committee resumed at 4:10 p.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Addison, Cameron (*Nanaimo-Cowichan-The Islands*), Chrétien, Clermont, Comtois, Fulton, Gilbert, Gray, Laflamme, Lambert, Leboe, Lind, More (*Regina City*)—(13).

*In attendance:* Messrs. David W. Slater, Professor of Economics, Queen's University; C. F. Elderkin, Inspector General of Banks; Denis Baribeau and Miss M. R. Prentis, research assistants.

The Chairman introduced Mr. Slater, who summarized his brief. In accordance with the resolution passed at the meeting of October 13, 1966, the brief is attached (*See Appendix X*).



At 5:00 p.m. the Vice-Chairman took the Chair, and at 5:30 p.m., the Chairman resumed the Chair.

The questioning continuing, at 6:00 p.m., the Committee adjourned until 8:00 p.m. this evening.

#### EVENING SITTING

(62)

The Committee resumed at 8:12 p.m. this day, the Vice-Chairman, Mr. Laflamme, presiding.

*Members present:* Messrs. Cameron (*Nanaimo-Cowichan-The Islands*), Clermont, Comtois, Fulton, Gilbert, Laflamme, Lambert, Leboe, Lind, Monteith, More (*Regina City*)—(11).

*In attendance:* The same as at the afternoon sitting.

Questioning of Mr. Slater was continued and concluded.

On behalf of the Committee, the Vice-Chairman thanked the witness who was permitted to retire.

At 10:15 p.m., the Committee adjourned until Thursday, December 15, 1966, at 11:00 a.m.

Dorothy F. Ballantine,  
*Clerk of the Committee.*

## EXTRACT FROM THE MINUTES OF PROCEEDINGS, DECEMBER 8, 1966

The Chairman presented the Seventh Report of the Sub-Committee on Agenda and Procedure, which is as follows:

Your sub-Committee on Agenda and Procedure met at 1:00 p.m. this day and has agreed to recommend as follows:

- (a) That briefs from the undermentioned, received after the deadline of November 1st, be accepted by the Committee: Prof. E. P. Neufeld, University of Toronto; Canadian Federation of Agriculture; A group of Twelve Trust Companies;
- (b) That briefs received from the undermentioned, who have indicated they do not wish to appear, be circulated forthwith to the members and published in the final issue of the Minutes of Proceedings and Evidence on the banking legislation: Canadian Chamber of Commerce; S. A. Bensch, Nanaimo, B.C.; Lloyd H. Denning, A.P.A., Dunnville, Ontario; James M. Dever, Montreal; H. Latulippe, M. P.; Alex Mills, C. L. U., Toronto; A. M. Moore, Dalhousie University.
- (c) That the following be invited to appear before the Christmas recess: H. H. Binhammer, Royal Military College, Kingston; R. Caterina, Carleton University; Canadian Credit Men's Association, Ltd., Toronto; E. P. Neufeld, University of Toronto; David W. Slater, Queen's University; Jacob S. Ziegel, McGill University.
- (d) That the Chief of the Committees and Private Legislation Branch be authorized to engage the services of reference index personnel for the purpose of indexing Proceedings on the banking legislation now before the Committee when it is printed in "blue book" form;
- (e) That on Thursday, December 8th, the Committee consider Bill S-30, An Act to incorporate League Savings and Mortgage Company.

On motion of Mr. Wahn, seconded by Mr. Fulton, the report was *approved*.

The Chairman stated that pending approval by the Committee tentative arrangements had been made for the following to appear on the dates mentioned:

Professors Binhammer and Slater on Tuesday, December 13th  
Processors Neufeld and Ziegel on Thursday, December 15th  
Professor Caterina and representatives of the Canadian Credit Men's Association Limited on Tuesday, December 20th.

Reverting to the Banking legislation now before the Committee, the Chairman tabled the following papers provided by the research assistants in answer to questions raised by members:

The Regulation of Foreign Banks in the United States, by Professor Jack Zwich, Columbia University,

A study of foreign banking operations in the United States prepared by Professor Zwick for the Joint Economic Committee of the United States.

Bank of Canada Statistical Summary, November 1966.

*Ordered*,—That the papers listed above be distributed to the members and that the Bank of Canada Statistical Summary be distributed monthly.





## EVIDENCE

(RECORDED BY ELECTRONIC APPARATUS)

TUESDAY, December 13, 1966

The CHAIRMAN: Gentlemen, I will now call the meeting to order. Our witness this morning is Dr. H. H. Binhammer. Dr. Binhammer is Associate Professor of Economics at the Royal Military College in Kingston. He received his Bachelor of Arts degree at Western. His Master of Arts degree at Queens and his Doctorate at McGill. That seems to be a very powerful combination of Canadian academic institutions. His specialty is in the areas of money and banking and international trade. I have explained to Dr. Binhammer that our procedure is to invite the witness to present his brief in summary fashion and then, of course, we proceed to our questioning. He has been kind enough to prepare an opening statement which I have just had distributed. Doctor, I would ask you to present your opening statement and then we will proceed with our questioning.

Mr. H. H. BINHAMMER (*Associate Professor of Economics, Royal Military College*): Thank you, Mr. Chairman.

I welcome and appreciate the opportunity to appear before this Committee. The brief which I submitted to you concerns itself with the deposit insurance schemes in the United States and attempts to draw out inferences for Canada.

To-day there are two major deposit insurance systems in the United States; one is administered by the Federal Deposit Insurance Corporation, the other, by the Federal Savings and Loan Insurance Corporation. All federally chartered commercial banks, and state chartered banks which can meet the entrance qualifications and which join, are members of the Federal deposit Insurance Corporation. On the other hand, all federally chartered savings and loan associations, and thrift type institutions which take deposits from the public, as well as all other similar institutions not chartered by the federal government and which join after meeting the entrance requirements, are members of the Federal Savings and Loan Insurance Corporation. In practice, the operations of both these institutions are similar, and since the details of the structure and operations of these institutions are found in my brief, I shall not deal with them at this time, but will be pleased to answer any questions that the members of the Committee may have.

I think what is perhaps of immediate concern to this Committee is to know why deposit insurance was introduced in the United States, and if for these reasons, or others, it should be introduced in Canada. Deposit insurance in the United States was introduced after the weaknesses of a banking system composed of thousands of small independent banks chartered by a multiplicity of legislatures came to light. It was a method of retaining the American type of banking structure by restoring confidence in the banking system and thereby stop runs on the banks. This was done by providing limited protection for depositors who were not in a position to judge the quality of a bank, and to

provide supervision and examination of banks without the fear of federal interference with states rights. Commercial banks were quick to join the Federal Deposit Insurance Corporation as the public whose confidence in banks had been shaken sought out banks who became members of the insurance scheme. The same psychological factors which played such an important role in inducing commercial bank which did not have to join to become members of the Federal Deposit Insurance Corporation still persist to-day. With the public confidence that Canadian chartered banks enjoy as a result of years of prudent management and government supervision, I do not think that they would voluntarily join a deposit insurance system. I doubt whether they would deem it necessary to attract customers as is the case in the United States.

The success of the Federal Deposit Insurance system in the United States paradoxically has not been the result of the insurance it provides *per se*. Its real success has been in the lead it took in introducing necessary supervision, examination, and regulation of the multiplicity of American banks. Its function in this area has now become to a large extent redundant since there has been a large proliferation of competent examining bodies.

During its 32 year history the Federal Deposit Insurance Corporation has dealt with 459 cases of failing banks. At the end of 1965 there were 13,876 banks insured by the Corporation. In 275 of the failing cases the Corporation made payment of deposits up to the insured maximum and in the other 184 cases it used the "deposit assumption" method which protects the depositors in full and makes their deposits available immediately. Under this procedure the Corporation acquires by purchase or loan, the assets of the distressed bank which are unacceptable to an absorbing bank, enabling the latter to assume the liabilities of the distressed bank. Up to the end of 1966 total net losses of the corporation were only \$43.3 million. These relatively small net losses have been due to the Corporation's attempts to "salvage" distressed banks rather than allow them to go under. I would think that in Canada where we have only a few commercial banks and which are relatively large, any method deemed necessary to protect or guarantee depositors accounts in the chartered banks should be concerned primarily with the prevention of bank failures. The failure of a bank, even though deposits were paid to an insured maximum would have serious repercussions on our economy. However, I feel that with the safeguards we already have the contemplation of a bank failure appears to be essentially academic. In short, I do not think a commercial bank deposit insurance system, following the American system, or for that matter any other such system, is necessary. If we are concerned over the safety of our banking system there are better methods for making it "failure-proof".

Now let me turn to the so-called near banks. These include deposit-taking financial institutions whose main business is still that of gathering-in the savings of the community and making them available for home mortgage-lending. In the United States these include by and large the savings and loan associations and the savings banks. In Canada I would include the trust and loan companies and the Caisses Populaires and the credit unions. This list, of course, is by no means complete.

The Federal Savings and Loan Insurance Corporation in the United States insures the deposits of thrift type financial institutions which take deposits from the public. To the end of 1965, after 32 years of operation it handled only

57 cases involving a loss. In 49 of these the distressed institutions were rehabilitated or merged, while the remaining eight passed into receivership. At the end of 1965 the Corporation insured 4,508 institutions. During its 32 year existence net insurance losses were \$68.4 million. The relatively few cases with which the Corporation has had to deal is in no small way the result of the examination, supervision and regulation provided by it. But, more important, is probably the role played by the Federal Home Loan Bank System. This system has been referred to as a central-mortgage banking system which stresses the co-operative principle. It is composed of 11 regional banks which act as "lenders of last resort". I mention the Federal Home Loan Bank System at this time because aside from its purpose already mentioned it also has the responsibility to stabilize home financing and to prevent booms and depressions in housing and mortgage markets. The Economic Council of Canada in its recent report has drawn attention to the problems in our own housing and mortgage market.

Now, I believe it is imperative that we find a way in Canada to provide adequate supervision and regulation of those institutions we refer to as the near banks. One way to do this would be to establish a deposit insurance corporation along american lines. However, since the psychological factors which have induced American institutions to join deposit systems do not appear to exist in Canada, I doubt whether Canadian institutions would voluntarily join unless other inducements are provided. May I suggest that these other inducements be lender of last resort privileges. In other words, let us consider establishing at the federal level an institution which would act as a lender of last resort for the near banks and at the same time have the responsibility for stabilizing the housing and mortgage market. As with the federal home loan banks in the United States all of its stock eventually could be held by the near banks. Initially the federal government would probably have to be financial participant. For the near banks to enjoy the privileges extended by this new institution they would have to subscribe to its stock and to meet minimum entrance qualifications. Moreover, they would come under its continual supervision.

My proposal here is a variation of one I made in a brief to the Porter Royal Commission. In that brief I suggested the establishment of a central mortgage bank within the framework of the Central Mortgage and Housing Corporation. My proposal to you today is a modification of my earlier one. In short, I recommend the creation of a federal institution, perhaps within the framework of C.M.H.C., that would provide adequate supervision and regulation of all our near banks and at the same time provide these institutions with sufficient inducement to accept such supervision and control. Moreover, such an institution might have a valuable part to play in stabilizing the housing and mortgage market.

The CHAIRMAN: Thank you, Dr. Binhammer. Now I suggest to the Committee that we follow our usual procedure. There is a basic theme, obviously, both in Dr. Binhammer's opening statement and in his brief which has been circulated and has been available for study by the committee for some days. Following this, of course, we will be able to ask Dr. Binhammer any questions we wish about other matters relevant to our order of reference. I will recognize members of the committee in the usual way; Mr. Laflamme followed by Mr. Lambert.



Mr. LAFLAMME: Mr. Binhammer, in your recommendations you recommend the creation of a federal institution that would provide adequate supervision. I think as you have stated in your summary, that you do not worry too much about having insurance for banks but precisely for so-called near banks. Did you make any study of the situation with respect to the constitution which in my view would require the participation of the provinces in such a scheme?

Mr. BINHAMMER: My position is that one way the Americans attempted to get around the problems of disputed jurisdiction was to create institutions at the federal level which state institutions could voluntarily join. It was strictly on a voluntary basis to join. Perhaps this is the way we have to attack it in this country.

Mr. LAFLAMME: On a voluntary basis. What if they do not?

Mr. BINHAMMER: This is why I think we have to have sufficient inducements to make it advantageous for them.

Mr. LAFLAMME: What do you mean by a kind of inducements?

Mr. BINHAMMER: By inducements I mean perhaps lender of last resort privileges. In other words, federal institutions that will make loans to these near banks from time to time either on a lender of last resort basis or perhaps on the basis of at the same time trying to provide a sufficient amount of money for stabilizing the housing and mortgage market.

The CHAIRMAN: Now, Mr. Lambert, and I might add I have Mr. Cameron followed by Mr. Addison on my list.

Mr. LAMBERT: Following up what Mr. Laflamme might have been suggesting as the constitution problem in this country, is not the control of banking in the United States much more of a state's right operation than it is in Canada; that is, constitutionally?

Mr. BINHAMMER: I think I would not want to make a dogmatic statement about that because I am not sure. I think the states probably have more rights when it comes to banking and money matters than is the case here in Canada.

Mr. LAMBERT: Well, you know what the provision in the constitution is here in Canada, in the BNA Act which says that exclusive jurisdiction shall lie with the federal government in the matters of currency and banking, period.

Mr. BINHAMMER: Yes.

Mr. LAMBERT: This does not apply in the American constitution.

Mr. BINHAMMER: No.

Mr. LAMBERT: So, therefore, there is a distinction at that point and, therefore, the point of departure in Canada could conceivably be different from that in the United States.

Mr. BINHAMMER: Yes.

Mr. LAMBERT: I have just completed reading an article by Dr. Zwick on the operations of foreign banks in the United States which illustrates very clearly that distinction of authority as between the states and the federal authority and how in actual effect a state is able to prevent a foreign bank from operating by simply not permitting it to join under the insurance scheme and

that is all there is to it. You do not tell people they cannot operate. You simply say you cannot get deposit insurance and that is the answer, then. That is a simple way of effectively cutting off any operation by a foreign bank. Now, coming back to the proposed Canadian scheme, in the United States, as you pointed out in your paper, the participation in the scheme is voluntary except in California where to operate as a bank you must be a member of the F.D.I.C.

Mr. BINHAMMER: May I add here that it is not voluntary for federally chartered institutions.

Mr. LAMBERT: In the United States, no. Therefore, there would be a parallel in Canada if what we understand is likely to be the government legislation that any federally incorporated or chartered bank or near bank will have to participate in the deposit insurance scheme. But does that not result in Canada, as you pointed out in your paper, in the fact that those institutions which do not need, shall we say, the protection of insurance are the ones who are being forced into this scheme and they are in there to help insure their competitors the near banks?

Mr. BINHAMMER: I think you interpret my feelings on this matter correctly, yes.

Mr. LAMBERT: In other words, the chartered banks and the federally incorporated trust companies would simply be shoring up their chief competitors, the near banks?

Mr. BINHAMMER: In so far as they provide the insurance fund which protects all the members, yes.

Mr. LAMBERT: Yes, to that extent. Now, what about the inducements to join? Do you think there is a sufficient inducement, say, for instance, a Caisse Populaire or credit union, which is at the far end of the spectrum of the near banks; it is far removed from the federal government and merely that it could advertise our deposits are insured up to a certain level—

Mr. BINHAMMER: I do not think that in Canada the mere fact of hanging a sign in your door and saying that you are being insured by a certain government insurance corporation will attract customers.

The CHAIRMAN: Why not?

Mr. BINHAMMER: Because, particularly in so far as a large majority of our near banks are concerned, they have a reputation. They have the confidence of the public already.

The CHAIRMAN: What about in today's climate the failure and difficulty of certain near banks?

Mr. BINHAMMER: I do not think it has come to a crisis proportion as yet. I think people will forget the recent incidents very quickly. I think that in the long run if we have more failures of the kind we have been experiencing well, then, certainly insurance would be an incentive.

Mr. LAMBERT: The point is that Atlantic Finance and Prudential Finance were not near banks.

Mr. BINHAMMER: Unfortunately, this is true.

Mr. LAMBERT: Therefore the only thing that Atlantic Acceptance was tied in with was British Mortgage and Trust. But there is no sign yet that Prudential Finance was involved with any near bank. Therefore, I doubt whether there is a crisis of confidence with regard to certain near banks. I am wondering just what the value of any insurance scheme is if it is merely the payment of an insurance premium for confidence unless there is, as you suggest in your paper, the necessity of very strict supervision. In other words, to get that certificate of insurance there will be a lot more than paying a fee?

Mr. BINHAMMER: Yes; I think we must be very careful to recognize that an insurance scheme without supervision and regulation is bound to failure. This is the experience with the American states. Many of the American states had their own insurance schemes but they did not have sufficient supervision. So, of course, most of these schemes ran into trouble.

Mr. LAMBERT: If the supervision and control are to be the backbone of any insurance scheme, and any near bank does not want to submit to it and you have said, and I agree with you, that the inducement to advertise that they are federally insured in so far as their deposits are concerned, is weak, then all I can see that at the present time anyway all the near banks will be almost unanimous in staying out.

Mr. BINHAMMER: Yes, unless you provide inducements of the kind I suggest one might consider.

Mr. LAMBERT: Well, what you suggest is a novel idea, this bank of last resort. I think it is a good idea.

To go to the last area of questioning I have at this time, Mr. Chairman, I believe the federal Savings and Loan Insurance Corporation, to which you referred on page 4 of your paper, this year inaugurated a first step in so far as it was concerned, and that is that savings and loan corporations in the United States had a ceiling imposed upon the interest rate they were allowed to pay on term deposits in order to eliminate, shall we say, the pell mell competition. I believe it was some two or three months ago, perhaps less than that, that the insurance corporation ordered a roll back to a ceiling of 5 per cent on term deposits or you would call them debentures or guaranteed certificates or what have you. Do you also feel that that should be a provision within an insurance deposit scheme; that the power be granted to this corporation that it could move to limit the interest payable by any member.

Mr. BINHAMMER: If you give the near banks the privileges of borrowing from a lender of last resort, the federal institution you create, then I think you can give this institution quite extensive powers. On the other hand, I do not know how far you can go if you create a deposit insurance corporation as such that is just interested in insuring deposits. You must give them sufficient power to supervise and control. How far you want to go along these lines I do not know. For instance, I do not know if you would want to give them as much power as you suggest.

Mr. LAMBERT: This fall, is the first time this has been tried in the United States, according to my information.

Mr. BINHAMMER: Yes.

The CHAIRMAN: Are you through?



Mr. LAMBERT: That is all, thank you Mr. Chairman.

The CHAIRMAN: Mr. Cameron?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, Mr. Binhammer I was interested in your proposal about establishing an institution which would serve as a bank of last resort, I suppose you might call it. I presume that you are envisaging an institution that will perform the same sort of function for the near banks that the central bank performs for the chartered banks?

Mr. BINHAMMER: Yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Is this a correct analogy. Is it possible to set up another central bank in any real sense of the word?

Mr. BINHAMMER: It has been done in the United States. The Federal Home Loans System is in a sense a central banking system for the near banks. But I think the difference between the central bank, as such, and the Federal Home Loan System which looks after the near banks is that the Federal Home Loan System in the United States is more concerned with providing lender of last resort privileges to provide the liquidity for these institutions in case of crisis and at the same time to provide them with sufficient funds in their housing and mortgage operations. The near banks in the United States are still strictly, on the one hand, thrift institutions and on the other hand investing their funds in residential mortgages.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): What are the source of the funds they supply to these institutions for their lending operations? Is it public funds?

Mr. BINHAMMER: The Federal Home Loan Banks and there are eleven, are owned by the member institutions. They buy stock in these banks, although the management as such, or the board that controls them, is government appointed. The funds they provide, they provide short-term funds on the basis of from 30 days to a year. They provide long-term loans up to 10 years. Now, there has been a suggestion, and they re-assessed the position over the last year or so, that the member near banks were relying too much on the funds they could get from the home loan banks. Now they have re-assessed it more in terms of making it a lender of last resort privilege than another government institution that actually provides them with funds to do their own mortgage business.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It seems to me there is a distinct difference between the operations of a real central bank and such an institution as you suggest. Of course when, and it has been very seldom, our central bank acts as a lender of last resort the chartered banks are not the source of the funds that are used, are they?

Mr. BINHAMMER: No.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No. Whereas, in your scheme, they would be the source of the funds; the subsidiary bodies would be the source of the funds?

Mr. BINHAMMER: Yes. There are a lot of variations one could have. For instance, this new institution that one creates could, perhaps, have lender of last resort privileges from the Bank of Canada.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Now you are making the Bank of Canada the lender of last resort.

Mr. BINHAMMER: Well, this way you could use new money, in a sense, to finance your mortgage markets if you wanted to.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Are you not really suggesting that these near banks should be established as regular chartered banks if, you are going to have that relationship with the central bank?

Mr. BINHAMMER: Not really; I think that one can have two kinds of banking systems, the so-called chartered banking system and the so-called near banking system. But, the difference in the two is that the prime function of the chartered banking system is providing payment mechanism in the economy. The near banks emphasis should be towards thrift institutions that provide funds on a long term basis, not commercial funds, but funds on a long term basis. Traditionally, as I say, they have always done this in the home mortgage field. I think this is a good place for the procedure.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The thing that interests and rather disturbs me is your suggestion that you might have as the next step in that, the central bank; our central bank acting as the lender of last resort gives me concern and I fail to see how you can do this unless you are going to establish them on the same footing as the chartered banks.

Mr. BINHAMMER: Well, as I say, this is a variation. One can have many variations here. I do not know if I would entirely endorse the idea of having the kind of institution I have in mind, have lender of last resort privileges from the central bank.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then you did make reference to the probable necessity for the federal government to be a financial participant in this new institution of lender of last resort. You said something which I did not quite understand, namely, that it should operate within the framework of the Central Mortgage and Housing Corporation. Did I understand you correctly?

Mr. BINHAMMER: I suggested that it might operate within the Central Mortgage and Housing Corporation. It could be another arm of the Central Mortgage and Housing Corporation.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then, does not your suggestion mean that you would have public funds channelled through the Central Mortgage and Housing Corporation to private lenders?

Mr. BINHAMMER: Yes; this would be one of the roles for stabilization purposes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would you explain exactly what you mean by stabilization purposes.

Mr. BINHAMMER: This would mean that since we must find some method of regulating the flow of money, this is available for residential mortgage lending. I think it is because of this erratic flow that we have had that we have had some

erratic fluctuations in housing construction which I think we perhaps can find methods of eliminating or at least dampening.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): If these institutions and near banks are, as you seem to feel, likely at some time to find themselves requiring more funds than they can get from the public, then, are you not suggesting that the purposes for which the Central Mortgage and Housing Corporation was established are going to be undercut. If we are going to inject public funds in there why should they not be injected directly through the Central Mortgage and Housing Corporation, as they were for a period when they made direct loans, and not passing it on to private lenders to pass out to the public.

Mr. BINHAMMER: I think what I had in mind here is that presently the Central Mortgage and Housing Corporation receives the money it lends out directly from the government. I would envisage that in the future you would have a new institution that would in turn provide Central Mortgage and Housing with funds. This new institution's own funds would come perhaps from selling its own debentures and its own bonds in the market. It would perhaps come from direct grants from governments, too. This new institution would be responsible for determining the amount of funds it would flow into the mortgage market at a given time.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It seems to me that you have here a conflict of two concepts of handling public funds. I call your attention again to what you said initially that the federal government will probably have to be a financial participant. To what extent do you envisage this and for how long?

Mr. BINHAMMER: I think under any scheme, even under a deposit insurance scheme, the federal government would initially have to make a grant or a loan—let us put it that way—to the corporation. This was the case in the United States both with the federal deposit insurance and the loan insurance scheme. You have to have a fund to start with. How large this fund would have to be I do not know. The present feeling in the United States is that the fund for insurance purposes should be about one per cent of total deposits of the institutions which are members of the insurance scheme.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You advanced the idea of this institution to be a lender of last resort finally as a means to induce these near banks to enter the deposit insurance plan. Now you appear to have gone further than that. You have gone quite beyond the mere establishment of a fund for deposit insurance to having public funds channelled into the hands of private lenders, and, as far as I can see, short-circuiting the operation of the Central Mortgage and Housing Corporation which has in the past confined itself either to guaranteeing the loans of private lenders, but they had to produce the funds themselves, or direct loans to those who seek loans for building purposes. This seems to be a certain conflict.

Mr. BINHAMMER: I would say that the Central Mortgage and Housing Corporation would still be the only institution that would make direct loans. This new institution I have in mind would be an institution which would be responsible for financing in one sense the direct loans and in the other sense providing



lender of last resort privileges to the near banks. The new institution I have in mind would not make direct loans.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No, I know it would not. That is just the point.

Mr. BINHAMMER: For instance, one could do what they have done in the United States. One could require that the near banks which belong to the new institution would have to hold a certain amount of the stock of the new institution, so this would be a source of funds. The new institution could sell its own obligations in the market. This would be another source of funds. The new institution could get funds perhaps directly from the government.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Dr. Binhammer, it still seems to me that what you are proposing in your last remark is that public funds should be made available to private lenders to lend in their lending operations, which seems to me a very strange concept.

Mr. GILBERT: Would that not also involve a spread of interest rates between the C.M.H.C. and the private lenders? Here you have public funds going to private institutions and the public then having to pay a wider range of interest rates than they would if they were obtaining the mortgage directly from C.M.H.C.

Mr. BINHAMMER: I think that perhaps you may be over emphasizing the public funds aspect of this. I can see the use of public funds only in so far as the government may deem it necessary to inject additional money into the market which we are doing at the present time under the C.M.H.C. plans. If this thing is successful I would think that the government funds perhaps might play a very minor role in financing this new institution.

(Translation)

The CHAIRMAN: Do you have other questions, Mr. Laflamme?

(English)

Mr. LAFLAMME: With the permission of Mr. Cameron, if the near banks do not want to have a loan from the federal government, if by the fact of obtaining a loan they have the right to control or to supervise the institution, then the other party can refuse it.

Mr. BINHAMMER: That is correct. The system would not work if you were thinking of making it primarily voluntary.

Mr. LAFLAMME: When and how could a loan be made under those circumstances, only if the near bank or the other financial institution is going to be bankrupt or—

Mr. BINHAMMER: I would suggest that this new institution I have in mind would provide liquidity to the near bank as required or if necessary.

Mr. LAFLAMME: Yes, but if the near bank needs liquidity it is because its financial situation is in jeopardy.

Mr. BINHAMMER: Not necessarily.

Mr. LAFLAMME: Why?

Mr. BINHAMMER: I would hope that there would be enough supervision and control to ensure that this would not be a case.

Mr. LAFLAMME: In my view it is a very hard way to get some kind of control.

The CHAIRMAN: Do you have further questions?

Mr. LAFLAMME: No.

The CHAIRMAN: Dr. Binhammer, this question may have been dealt with when I stepped out for a moment to attend the labour committee which is meeting across the hall, but could you give us some indication of why there turned out to be two separate systems in the United States. There is one for what they call banks and there is one for what they refer to as the thrift or savings and loans institutions. How did that come about? Was there some constitutional or historical reason?

Mr. BINHAMMER: They already had a home loan banking system that built the insurance scheme under the federal home loan banking system. I am sorry, I cannot give you a specific answer to that question.

The CHAIRMAN: I gather in the United States they have about 12,000 banks and probably a large number of savings and loan institutions. In Canada we have eight chartered banks and probably 100 or nearly 200 near banks. The United States seems to have had a history of proliferation, as you point out yourself, of inspection and supervision and so on in this financial field. I wonder if you could indicate why it would not be simpler, both administratively and also from the point of view of cost, if we are to have insurance schemes, to have one scheme for all institutions which might be able to have different rates and different rules for different kinds of financial institutions. Would that not be a more direct response to the more limited Canadian situation?

Mr. BINHAMMER: Perhaps, if you can sort out the different rules for the different organizations and different rates for the different organizations, but this may be a bit of a problem.

The CHAIRMAN: But there is no reason why it cannot be done by one institution rather than two.

Mr. BINHAMMER: No.

The CHAIRMAN: I suggest, considering the fewer number of institutions in the public sphere in that area, in Canada business might be administratively more simple and also cheaper having two separate supervisory and lending institutions.

Mr. BINHAMMER: I would like to see the banks and the near banks kept separate unless you follow the Porter Commission and bring the near banks and group banking functions within the ambit of the Bank Act.

The CHAIRMAN: Why would you like to have them kept separate?

Mr. BINHAMMER: Because I think they are either in or out. You have to make a decision as to what you want. You either have them in or you have them out.

The CHAIRMAN: But if you have different rates based on experience or type or risk and so on would that not meet your objection that the chartered banks have a certain solidity and so on and are unlikely to call upon the deposit insurance institution in the same way that some of the other financial intermediaries might have to do, and also different rules.

Mr. BINHAMMER: There is another problem involved here. Do you suggest that the chartered banks be allowed to join on a voluntary basis and, if so, what inducements do you have for the chartered banks?

The CHAIRMAN: I do not think that there is a voluntary question here. If you follow the American experience—the United States equivalent of our chartered banks have to join the federal reserve system. With respect to your suggestion about the near banks holding stock, and so on, did we not try that once before with the Bank of Canada when we set it up?

Mr. BINHAMMER: Initially, yes.

The CHAIRMAN: Initially. Why did we depart from that?

Mr. BINHAMMER: I think there is a big difference between a central bank looking after—it is the centre of our entire banking system and what I have in mind here looks after the near banks.

The CHAIRMAN: But is not what you have in mind for the near banks the equivalent within that sphere of the Bank of Canada for the chartered banks, with respect to being a lender of last resort.

Mr. BINHAMMER: Yes. The only difference there is that the central bank as such, its liabilities are in fact money. It can create—

The CHAIRMAN: If you proposed institution provides liquidity for the near banks will it not provide them with money?

Mr. BINHAMMER: Yes, but the central bank controls new money into the system. This would not be possible for the bank I have in mind here.

The CHAIRMAN: Why not? If it permits the near banks to expand their credit based on the liquidity provided them by your proposed institution would it not be throwing more money into the system?

Mr. BINHAMMER: No, not the same way as the central bank.

The CHAIRMAN: Yes. I just have one or two more questions before I recognize Mr. Addison.

In the United States, I seem to note that from time to time there appears to be conflictalities with respect to monetary policy between different instruments of the federal government in that area and the administration itself. What would be the effect on control by the government itself, which must be responsible to the public for this sort of thing, on monetary policy if you have these two institutions? Especially, I might add, if the one you propose is owned completely by the near banks.

Mr. BINHAMMER: The near banks own all of its stock but, I would suggest, as in the United States—for instance, the president with the consent of the Senate appoints the directors—that in Canada the government would appoint the directors of this particular institution. We would make sure that there is close



liaison in the work of this institution and the Department of Finance and the Bank of Canada.

The CHAIRMAN: Yes, but we have one experience in the last several years when the system was just based on close liaison rather than direct accountability which is the law. There are amendments which we are about to study with respect to the Bank of Canada Act to deal with that problem. Does that not indicate that your proposal might lead to some problems of control of the monetary policy by the government?

Mr. BINHAMMER: No, but it could, yes.

The CHAIRMAN: Judging from a recent Canadian experience, which I will not go into, but which we are all aware of.

Mr. BINHAMMER: Yes, but I think we have learned that we can write certain things into legislation that may prevent this sort of thing happening.

The CHAIRMAN: Do you suggest then that it be made clear in the legislation that the administration of this institution you are proposing must follow the lead of whom the government, or the Bank of Canada?

Mr. BINHAMMER: Well, in the final analysis it must be the government.

The CHAIRMAN: Now, one final point, with respect to the institution that is covered by the Federal Home Loan Bank System, and so on, are they not more narrowly limited to the housing lending field than our near banks are?

Mr. BINHAMMER: They are moving in the same direction as our near banks have been moving; as a matter of fact they may have moved a little further even than our near banks in taking deposits from the public.

The CHAIRMAN: But as far as what they do with the deposits are our near banks not operating in a wider sphere than the thrift institutions in the United States, as far as lending is concerned. They lend over a wider range—

Mr. BINHAMMER: No, their lending is confined primarily to the residential mortgage market.

The CHAIRMAN: Our near banks?

Mr. BINHAMMER: In the United States.

The CHAIRMAN: No, I am talking about Canada. I am suggesting that it would appear that the Canadian near banks are now lending over a wider sphere than the American ones.

Mr. BINHAMMER: Yes.

The CHAIRMAN: If that is the case, and if this is desirable, would that not lessen the weight of your argument for having a separate institution in Canada which would concentrate on the housing mortgage market?

Mr. BINHAMMER: I think it would; yes.

The CHAIRMAN: Mr. Addison?

Mr. ADDISON: Professor Binhammer, I would like to discuss the deposit insurance aspect of your brief. I would like to preface my remarks by an article that was in a report of the *Toronto Telegram* of Saturday, December 10 entitled

"Deposit Insurance", and the headline reads "Public may have to pay". It goes on to say:

If deposit insurance legislation is eventually introduced, its cost is likely to be passed on to that already burdened figure—the general public.

It also goes on to say, and I am quoting Mr. Kenneth Burn the vice-president of Eastern and Chartered Trust Company:

"If it is established at an unrealistically high rate, it means that the companies are being taxed. If such were the case, this taxation would be passed on to the public by means of a reduction in the rate of interest being paid," he said.

Then he goes on:

He told the Rotary Club's weekly luncheon that the best protection for investors lies in sound management practices and not in further regulation.

Now, we had the opportunity of questioning the Canadian Bankers' Association with regard to the proposed federal deposit insurance, which appears to be almost a *fait accompli*; I think, without question it is going to be introduced by the Minister of Finance, we hope before Christmas.

The CHAIRMAN: There would be legislative study, of course.

Mr. ADDISON: Yes. We have heard from the Canadian Banker' Association, and this gentleman representing a trust company. The feeling of these organizations seems to be that the cost is going to be unnecessarily high to the corporations and eventually to the public. I tried to make the point with the Canadian Bankers' Association that insurance schemes are normally predicated upon experience, and I do not think the federal government is out to create a great bonanza in so far as a profit making crown corporation with the federal deposit corporation is concerned. The primary purpose, as I see it, is to bring the near banks under federal control; and this is only one method. You said today, when Mr. Gray was questioning you, that it would be difficult to adjust the rates, I believe, for various classes. The Canadian Bankers' Association feel that they are going to have to, in effect, subsidize the smaller near banks. I cannot see the validity of your objections to a federal deposit system, other than the fact that the rates might be too high; and if there are no failures the rates cannot be high.

Mr. BINHAMMER: This business of rates, of course, has been a point for discussion in the United States for a long time; because the question is how large an insurance fund do you require to provide adequate protection. You do not know. In the American system, for instance, the federal government stands by with \$3 million in case deposit insurance requires additional funds. It is hard to say how much actually is required. Under normal conditions you are quite correct, the fund may not be very high at all. But surely, here we are worried about crisis conditions, are we not?

Mr. ADDISON: I do not think so. I think we are worried about every day situations, such as we have had with Prudential, such as we have had with British Mortgage and Trust; these are the conditions. We are not legislating yet for crisis, because there may not be any way of legislating to overcome that.

Mr. BINHAMMER: Well, I think that as far as the banks are concerned there are better ways to provide supervision and regulation right within the Bank Act without imposing a deposit insurance scheme. As far as the near banks are concerned, I would prefer a system of regulation and supervision that does not have deposit insurance, because from what we see in the United States of the insurance deposit schemes the heart of interest of these schemes is the supervision and regulation that they have provided; not in the insurance as such.

Mr. ADDISON: I appreciate that; there is no question about it. I think if the federal deposit insurance scheme was unconditionally guaranteed by the government there would not be any need to charge a premium. I do not think that we, as a country, want to see our financial institutions operate in an improper way. My only point is that here we are talking about a degree of cost. I do not think we are talking about a degree of principle, and that is that we want regulation over our near banks; and this is the only way we can get around it constitutionally.

Mr. BINHAMMER: But this is what the United States did; this is one way of getting around the constitutional hurdle.

Mr. ADDISON: And the carrot is the guarantee for the near banks to get them to come in.

Mr. BINHAMMER: I do not think we have the same carrot that they have in the United States. The carrot in the United States is the fact that the system was created in a period of panic, in a period of crisis. These psychological factors, which I pointed out, I think still persist today; but I do not think we have the same atmosphere in Canada at this time.

Mr. ADDISON: I watched a television program, I think it was on Channel 9, on Sunday evening, where one gentleman had lost, I think, \$10,000 which he had deposited with Prudential Finance Corporation. I would say it is a pretty serious matter when an individual invests his life savings in an institution and he loses it all.

Mr. BINHAMMER: Of course, when we speak about a crisis—

Mr. ADDISON: It is not a crisis, but I say that we must protect the public.

Mr. BINHAMMER: When we speak of finance companies, I think we are much closer to provincial jurisdiction than we are perhaps with loan and savings institutions.

Mr. ADDISON: As I understand it in the bill, and according to the *Globe and Mail* this morning, this federal deposit insurance corporation will be available to organizations such as Prudential Finance—deposit taking organizations.

The CHAIRMAN: Well, of course, this is a question of definition; we will have to go into, in due course, whether a firm such as Prudential, which calls itself a finance company, is really the same as the other finance companies which concentrate on the lending out of their money to consumers and do not seek funds from the public at large, which are secured by notes, or what have you. Your suggestion, Mr. Addison, is that in a sense an institution like Prudential is really more of a deposit taking institution like a trust company than, say, Atlantic Acceptance was.



Mr. ADDISON: Yes; because they are dealing with the public and say smaller denominations rather than the short term market where they are dealing with larger amounts of money.

Mr. BINHAMMER: Well I just would like to say I disagree with your premise that there should be an insurance corporation primarily for the protection of the public.

Mr. CHAIRMAN: I now recognize Mr. More, Dr. McLean and Mr. Gilbert.

Mr. MORE (*Regina City*): Professor, some of my points have been covered. Your brief indicates that both these corporations in the United States have 32 years of operation, so they were both started at the same time.

Mr. BINHAMMER: Yes.

Mr. MORE (*Regina City*): It is too bad but we cannot get the fundamental reasoning for having two corporations at that time. They did not follow each other. There was not a gap that brought on the two; they were instituted at the same time, apparently, but we do not know the reason.

The CHAIRMAN: Mr. More, perhaps we ask one of our research officers to look into that and have a report for us.

Mr. MORE (*Regina City*): As a matter of clarification, you speak in the one case of a net loss of \$43.3 million; in the other a net loss of \$16.4 million. By net loss, do you mean losses exceeding premium income.

Mr. BINHAMMER: No, the net loss is effected—in most cases these are salvage operations and after a merger has been effected or a company has been rehabilitated, the corporation then gets back any of the advances it may have made previously. The corporation for instance may buy some of the assets from an institution in distress. When these assets can be sold later, of course, the corporation recoups that amount of money.

Mr. MORE (*Regina City*): So this is a net loss to the corporation of the securities under the advances they made.

Mr. BINHAMMER: Yes.

Mr. MORE (*Regina City*): In other words, the total losses throughout their operation.

Mr. BINHAMMER: That is right, yes.

Mr. MORE (*Regina City*): There are no figures indicating the relationship to the deposit, to the premiums paid, or their years of operation, of these losses.

Mr. BINHAMMER: I am sorry, no.

Mr. MORE (*Regina City*): Is there no government money involved in meeting these losses? They have been met by premium—

Mr. BINHAMMER: Initially the federal government contributed \$100 million in the Federal Savings and Loan Corporation. It has received all this back. In the other institution, the Federal Deposit Insurance Corporation, the federal treasury initially contributed \$150 million and the federal reserve system \$139.3 million and all these moneys have been paid back, I might add, with interest. They were paid back in 1950-51.

Mr. MORE (*Regina City*): You take the position that any law requiring our present chartered banks to contribute to deposit insurance is unnecessary and an imposition on their cost of operation. I take it that that is your point of view.

Mr. BINHAMMER: Yes.

Mr. MORE (*Regina City*): I think I agree with it. They would be required to contribute earnings from their customers, from their income, to form the base for their competitors to operate on in this field, an unnecessary thing for our chartered bank system as it stands today.

Mr. BINHAMMER: This is my feeling.

Mr. MORE (*Regina City*): Now with respect to your suggestion of a bank of last resort and the statement that it would level out the housing market, I am not clear as to how this would be accomplished. Mr. Cameron's questioning on it seemed to indicate a bit of confusion—at least it left some confusion in my mind—as to your point of view of how this would be done. You suggest through C.M.H.C., but then government funds might be the framework within which this would be set up. You also said in answer to Mr. Cameron that C.M.H.C. would still continue to do this, so that their lending ability would depend on government policy. It could be turned on and shut off the same as now. How would the establishment of a bank of last resort overcome this and level out the funds available for the housing market. How do you envisage this being accomplished as long as C.M.H.C. is still subject to government policy, government operation?

Mr. BINHAMMER: I think perhaps we should not have mentioned C.M.H.C. Perhaps this muddled the water somewhat.

The CHAIRMAN: Without it, even, I would like to know how such institution could level out the lending in the housing field; never mind with C.M.H.C. at all.

Mr. BINHAMMER: I would suggest that in the way this institution makes funds available to the near banks, it could control to a degree the money that flows into the mortgage market. This institution which I, as a matter of fact, at one stage called the Federal Mortgage Bank, could sell its debentures or its own bonds in such a way that it could stabilize in a sense the bond market at times, or certainly assist in debt management. At other times the money that it raises would be available for the mortgage market.

Mr. MORE (*Regina City*): Professor, I think in Mr. Gray's questioning, you agreed with him that our near bank operations are far different from the near bank operations in the United States, primarily their funds go into the housing market. This is not the case in Canada, is it? Is it not a little far-fetched to say that, because of this institution and its participation it would increase and keep steady the flow of money into the housing market in Canada, regardless of government policy and C.M.H.C.

Mr. BINHAMMER: Well, the institutions I had in mind are trust and loan companies. Certainly they are still important institutions in the mortgage market, so is the Caisse Populaire, so are the credit unions. Now, I have not included the finance companies which are again something different.

Mr. MORE (*Regina City*): And you suggest that if these institutions now offered it under bank of last resort, the money market in regard to housing would not be what it is today in Canada.

Mr. BINHAMMER: I would hope so.

The CHAIRMAN: Now, I recognize Dr. McLean (Charlotte).

Mr. McLEAN (Charlotte): Professor Binhammer, banking in the United States is a great deal different from banking in Canada. They have the state banks which have certain privileges which the national banks do not have and the national banks have certain privileges which the state banks do not have. When the Chase National took over the Manhattan Bank they took the Manhattan Bank's charter although it was a state bank. It seems that you think if the government interfered in some way that we would have more housing by levelling the money market out. It seems that in the United States, they have all these institutions, but housing has gone down every quarter and they expect it to go down farther in the last quarter of this year. How do we explain that.

Mr. BINHAMMER: I think the explanation is that all these institutions we create are not going to be a panacea; they are not going to solve all our problems. All we can hope for is that they will assist us in solving some of our problems. We know that we should do something, perhaps, with the housing and mortgage market. I say that if we can at least make an attempt through the system that I have suggested towards stabilizing the housing market, fine and dandy. I am not suggesting for a minute that this is going to work the way one would hope it would work.

Mr. McLEAN (Charlotte): Professor, how can it work when they do not control interest rates? Are interest rates not at the bottom of the whole thing? Is not the federal system in the United States putting on the brakes? The same thing is happening in Canada, the United Kingdom, France, Germany—all over the world. Money knows no patriotism except in war. We are in peace now, and are interest rates not at the bottom of it? You cannot straighten it out unless you straighten interest rates out.

Mr. BINHAMMER: Interest rates are only a symptom. Interest rate is the price we pay for money, so in order to affect the price you have to affect the demand and supply of money. I do not think you can *per se* control an interest rate or a price, but you can do something about the demand and supply. This is what I have in mind here. With the money available for the residential mortgage market, you try to change in some way the flow of funds that enters this market.

Mr. McLEAN (Charlotte): Yes, but if the central banks are all in favour of not putting more money out and restricting credit, what good is your institution going to be?

Mr. BINHAMMER: The approach the central bank has to take, of course, is to control the total money supply. It takes a very impersonal approach and, as such, there are certain sectors of the economy—housing is one—that it hits very hard, perhaps more so than we want it to be hit from a social point of view. So now we impose another institution or some other method to help a particular area that we think needs assistance.

Mr. McLEAN (Charlotte): But how can you help it when it is the interest rate at the bottom that controls your money supply at the present time? There is only so much floating around and the interest rate controls it. You can have a good many institutions but that is not going to create more money; it is not going to help the situation so far as I can see. The chartered banks have been going



over 100 years and they have been doing a pretty good job. If they were to hang out a shingle tomorrow and say, "now our deposits are insured" would you not think that would show lack of confidence? Is it not confidence that was need at the present time?

Mr. BINHAMMER: I do not know that we show lack of confidence. I do not think it would increase confidence.

Mr. McLEAN (*Charlotte*): I have been going into banks for the last 50 years and if all at once I saw, "we are insured now, your deposits are insured" would not that make me think that there was some lack of confidence somewhere?

Mr. BINHAMMER: There might be such a perverse reaction among certain people, but I do not think it would be serious.

Mr. McLEAN (*Charlotte*): Again, do you not think that these institutions that take public money on deposit, should have some supervision somewhere?

Mr. BINHAMMER: Oh, I definitely do.

Mr. McLEAN (*Charlotte*): We are not getting that at the present time because they have provincial charters. How are we going to overcome this? It seems to me that we are not going to overcome it by making somebody else pay for it, like the chartered banks, and leading people to believe that we have a lack of confidence in the chartered banks, simply to save the near banks.

Mr. BINHAMMER: The trouble is, how are you going to supervise them, control them, regulate them on a federal level when you can do this only on a voluntary basis, as I see it, because of provincial jurisdiction? The only way to do it is to give them a carrot, and with this carrot they will join some insurance or supervisory system.

Mr. McLEAN (*Charlotte*): Would it not be better to leave the chartered banks alone and just deal with the near banks? The government could set up a system and say, "We are going to put \$50 million or \$100 million on deposit, and if you come in you are going to come in under that, and your rates are going to be very low, because we are going to put this \$100 million up", and get the near banks in under it? Then, if this were known to the public and these near banks were not insured, and it would be to their advantage to insure, it seems to me that something would be done about it. The near bank that was insured would get the preference, but it seems to me that the government would have to put up a much money in the first place, and not ask the people that are secure to pay the bill.

Mr. BINHAMMER: You suggest that the cost of any kind of insurance scheme for the near banks be shared by the federal government and the near banks?

Mr. McLEAN (*Charlotte*): Yes; but there need not be any cost if they have the proper supervision. They will not fail if they have the proper supervision and so the cost would be very low. We would have to pay the cost of the supervision, which is the main thing.

The CHAIRMAN: Do you have any further comment, doctor, on Mr. McLean's suggestions? If not, I presume that Mr. McLean would permit me to give the floor to Mr. Gilbert.

Mr. GILBERT: Mr. Chairman, my first question to Professor Binhammer is informational. I would like to know what percentage of the home and mortgage market in the United States is financed by the Federal Home Loan Bank System.

Mr. BINHAMMER: Pardon?

Mr. GILBERT: What percentage of the home and mortgage market in the United States is financed by the Federal Home Loan Bank System?

Mr. BINHAMMER: The Federal Home Loan banks, through the years, have been asked to finance a substantial amount of the residential mortgage market and, in fact, it was last year or the year before, when they decided that this was not their original purpose. Their original intent was to act as a lender of last resort; in other words, to give protection or liquidity to the so-called near banks. I understand they are retreating somewhat and becoming more a lender of last resort and less a prime source of funds for the mortgage market.

Mr. GILBERT: Let me direct your attention to the Central Mortgage and Housing Corporation. In the last report of operation for the year 1965 they indicated that home financing was 65 per cent sponsored by the conventional lenders and 35 per cent by Central Mortgage and Housing Corporation and in 1966—and as you have said we have had an erratic flow of mortgage moneys for the mortgage market and the home building market—the Minister in charge of that department said that it was the fault of the conventional lenders who did not go into the market. In other words, there was a reduction from the 35 per cent, and now C.M.H.C. has had to inject mortgage moneys into the housing field to build it up. Your scheme of things is to have the government lend public funds to these conventional institutions as a carrot to bring them in under this deposit insurance system. Are you suggesting that this is the way that we should determine our home and mortgage market here in Canada.

Mr. BINHAMMER: I suggest that this may be one way.

Mr. GILBERT: Would it not be better if the government took the direct initiative and became responsible for 65 or 70 per cent of the financing and let the conventional institutions take care of the balance?

Mr. BINHAMMER: I do not know. I think this is a policy decision of the government. I would not want to comment.

Mr. GILBERT: Your proposal is going to directly affect the interest rates because there is a spread of one per cent between C.M.H.C.—in fact more than one per cent. There is a spread between the C.M.H.C. rates and the conventional rates, and what you want to do is to give the conventional lenders more money, thereby maintaining the high rates, the spread.

Mr. BINHAMMER: The new institutions would have the discretion to decide when and when not to provide extra money to the near banks for mortgage purposes.

Mr. GILBERT: I think this is where control comes in. The basic problem has been this erratic flow of money and we have depended on the conventional lenders, 65 per cent according to C.M.H.C. report. Central Mortgage and Housing Corporation have come in at this stage to inject more money into the flow to try to stabilize the market. Can we depend on the conventional lenders to stabilize the market whether we offer them money or not? Does it not result in a higher interest rate?

Mr. BINHAMMER: I do not think it needs to result in a higher interest rate. It may in fact have the opposite effect in the long run. I think that one uses the interest rate to regulate the sort of flow of funds that you want to go to the mortgage market. Perhaps in this area we have not done enough.

Mr. GILBERT: Mr. Binhammer, my second question is with regard to the uniformity of rates that would be charged to banks and near banks with regard to deposit insurance. In your brief on page 8, you say.

If it is intended Canadian legislation is to encompass both the banks and the near banks, an assessment policy based on risks would be preferable to one based on deposits.

The question is, would you have uniformity or rates, or would you have one on risks because if it is on risks you have different risks with regard to banks from what you would have with regard to near banks.

Mr. BINHAMMER: This is the argument that is put up in the United States, that rather than have premium charge on total deposits, segregate your assets according to some formula and base your risks on these assets. This seems to be more equitable. However, the argument against it is how do you assess the risk of these various assets?

Mr. GILBERT: Especially if you are trying to induce the near banks to come in. If there is a spread of rates between banks and near banks, how can we pull in the near banks?

Mr. BINHAMMER: This is the problem that we have to face.

Mr. LAMBERT: Mr. Chairman, what about the word "insurance" that comes into this whole scheme? Surely, insurance is based on risk. The difference between Mr. Gilbert and myself as automobile drivers determines in many instances the rate that I am going to be paying as against his. Surely to goodness if you are going to insist on insurance, of course, the thesis you are advancing is most tenable.

The CHAIRMAN: You refer to risks. Are you referring to the risk of loss or the type of risk involved in the determination of the nature of the loans that the institution is making which is not necessarily exactly the same thing? What I mean is that if you applied this approach would this not mean that you are calling for a heavier burden of assessment on chartered banks that make the riskier commercial loans and yet are the strongest institutions, the terms of assets?

Mr. BINHAMMER: This is where the problem begins, of course. Are the total assets of the banks riskier or more subject to default and loss than the assets of the long second mortgages or third mortgages, or what have you, that the near banks hold?

The CHAIRMAN: In terms of loss. We are not taking about an institution's loss on a particular class of loan from year to year. We are talking about the possibility of the institution failing, not being able to meet its obligations to depositors from its own assets. If that is the case, it may be that I have not understood what you mean when you talk about risk but if it is the type of risk that the institution gets involved in, in its loaning business, then I suggest you may be calling for a heavier burden on those institutions which have the greatest



ability to meet obligations to depositors from their own assets. Do you have any comment on that?

Mr. BINHAMMER: Well, I think one must look at the history of the commercial loans made by the chartered banks and I think their loss experience has been very good as far as I can see on this, on this—

The CHAIRMAN: Mr. Gilbert, do you have anything further on this?

Mr. GILBERT: No, I think is all I have. Thank you, Mr. Chairman.

The CHAIRMAN: Now I recognize, Mr. Clermont.

*(Translation)*

Have you any questions, Mr. Clermont?

Mr. CLERMONT: Mr. Chairman, as I had to attend—

The CHAIRMAN: Is your system working now? Can you hear me? Are you getting the interpretation?

Mr. CLERMONT: Good. I was obliged to attend the Labour committee where they studied Bill S-35, clause by clause. So it will be difficult for me to figure which questions to put. My questions, perhaps have already been put. In any event, professor, according to the brief that you submitted to us, it would seem you do not favour a system of deposit insurance for chartered banks, but you do favour a system of deposit insurance for the near banks. Do you not think, professor, that if the Government were to establish deposit insurance only for near banks, this would create a certain uncertainty in the minds of the public? Would the public feel some uncertainty about this? Monsieur Lambert, if the financial institutions that are near banks, were to use the fact that their deposits were insured and the deposits of banks are not insured, is this not going to encourage deposits with the near banks?

Well you see, in my case, I am putting the questions, Mr. Chairman, I am not like others who answer the questions before they put them.

*(English)*

The CHAIRMAN: Dr. Binhammer, can you deal with the interesting point raised by Mr. Clermont?

Mr. BINHAMMER: If I understand you correctly, do you feel that the near banks may have an advantage if only they are included in a deposit field?

Mr. CLERMONT: To draw deposits from the public.

Mr. BINHAMMER: I do not think so. I think the confidence of the banks is such that if you have insurance for the near banks this will not in any way give the near banks a competitive advantage.

*(Translation)*

Mr. CLERMONT: It seems professor, that you would prefer another system over deposit insurance. You seem to favour a system that would enable the near banks to negotiate the securities of the Bank of Canada. Could you explain what you mean by this?

*(English)*

Mr. BINHAMMER: I think the real problem is that of providing some standard supervision and regulation of the near bank. Now, how do we do this, in so

far as we have to consider two jurisdictions, or what appears to be two jurisdictions, provincial and federal? One way is to have a deposit insurance scheme on a voluntary basis, because of the disputed jurisdiction, but how are you going to get the near banks to become members of an insurance scheme unless you provide them with certain advantages or certain privileges? I think one way of doing it would be to give them lender of last resort privilege at some institution. I did not say at the Bank of Canada. I suggested introducing or creating another kind of institution for this purpose as is the case in the United States.

(Translation)

Mr. CLERMONT: In your brief, Professor, you mentioned that you would establish a government corporation to handle the negotiables. This would, you say, create confidence in the public buying and encourage the public to deposit with the near banks. At the present time, do these near banks now attract public deposits, because they pay a higher interest rate on deposits from the public?

(English)

Mr. BINHAMMER: Yes, it is quite true at the present time they attract deposits from the public because of the interest rates that they can charge. On the other hand, it is because of their growth, their success in attracting more public deposits that we have become concerned with their safety, with the type of operation that they have.

The CHAIRMAN: Do we have any members in the Committee who have not taken part in the first round? If not, I recognize Mr. Lambert.

Mr. LAMBERT: Mr. Binhammer, I am having a little difficulty at the present time because we have not had the government scheme disclosed to us. One of the integral parts of the present scheme will be the participation or the non-participation, or the dovetailing of some proposed province of Quebec scheme, because the province of Quebec has indicated that its government will set up its own scheme and this brings me to the very knotty problem, and that is k-n-o-t-t-y, of how to deal with the two largest of the near banks, the Montreal Trust and the Royal Trust who are Quebec-based trust companies but whose operations by far and large outside of Quebec exceed the operations in that province. Now, I have not been able to determine what Solomon-like plan is going to operate to distinguish between the operations of the Royal and Montreal Trusts outside of the province of Quebec and its operations within the province, whether the province will insist on its scheme covering the deposits of those companies across the country. If it does, I can assure you that will be the quickest invitation for a transfer of head office for those two companies. Have you considered this sort of slippery condition which does not exist in the United States whose system you have studied and elaborated on to us.

Mr. BINHAMMER: This is what I am afraid of. If every province is going to come along with their own deposit system or insurance system, we are going to have chaos. You must have some centralization.

Mr. LAMBERT: Have you heard at all what the proposals are?

Mr. BINHAMMER: Only what I have read in the papers, and that is not very much.

The CHAIRMAN: Mr. Lambert, perhaps it might be helpful if we knew under which jurisdiction these two trust companies were incorporated.

Mr. LAMBERT: They are from the province of Quebec.

The CHAIRMAN: The Royal Trust and the Montreal Trust?

Mr. LAMBERT: Oh, yes.

The CHAIRMAN: They are provincially incorporated?

Mr. LAMBERT: Oh, yes.

Mr. BINHAMMER: Do they not have federal charters?

Mr. LAMBERT: No, neither of them.

The CHAIRMAN: Mr. Elderkin agrees.

Mr. LAMBERT: It is a very touchy point.

Mr. ELDERKIN: They hold provincial licenses in all the provinces in which they operate, but their charters are in the province of Quebec.

The CHAIRMAN: They are not under the supervision of the federal authority.

Mr. ELDERKIN: None whatsoever.

The CHAIRMAN: That is a very interesting point, Mr. Lambert.

Mr. LAMBERT: Well, that is all that I wanted to bring out. I do not know, maybe Mr. Laflamme has a supplementary point in this regard.

Mr. LAFLAMME: I have only one other question to ask Mr. Chairman, which, is this. What do you think of the deposit insurance system by way of having all guarantees given to the public for their money or by way of controlling the financial institution which would not fall under federal jurisdiction?

Mr. BINHAMMER: I think that you cannot have just insurance without control. I think what we are really interested in is the proper supervision of these institutions. One way of doing it, as the Americans have done, is to do it via the vehicle called deposit insurance.

Mr. LAFLAMME: Is the insurance project for the purpose of giving the public a guarantee for their money or is it a way of controlling the financial institutions?

Mr. LAMBERT: Or both?

Mr. LAFLAMME: Or both, I would think both.

Mr. BINHAMMER: Yes.

The CHAIRMAN: Before I recognize you, Mr. Cameron, I would just like to pose one or two brief questions to Dr. Binhammer. You have raised the point, as have various members, that there could possibly be an element of unfairness in asking the chartered banks to pay premiums for deposit insurance that they may well not need in the ordinary sense of the term. As you know, at the present time under the Bank Act the chartered banks must pay a tax or an assessment to the federal government to cover the cost of their inspection by the office of the Inspector General of Banks. Would the complaint of the chartered banks be the same if the assessment that they now have to pay was not required and instead they had to pay only a premium based on experience or risk which would take into account their strength and so on. Would that not balance off the cost factor fairly well?



Mr. BINHAMMER: In other words, as far as the supervision of chartered banks is concerned, this would remain with the Inspector General of Banks.

The CHAIRMAN: Well, they would continue to be supervised but I am raising this suggestion for you and for the Committee that right now they do pay an assessment required by the Bank Act to the federal government to cover the cost of their supervision, and quite rightly. If they are asked to pay a premium for deposit insurance in addition, they make the complaint and you can understand their argument, that this is an element of additional cost that they should not have to pay. If instead of having to pay both, they had to pay only one, would they not, in a sense, be in roughly the same position as they are now if the premium turned out to be not much different from the assessment? Is this not a possible answer?

Mr. BINHAMMER: Yes, but surely the premium would have to be higher than the assessment. You have to have funds first for supervision, but then you also need funds for insurance, the insurance fund *per se*.

The CHAIRMAN: But would not the amount required for insurance be rather limited in view of the nature of the risk of their failing? Mr. Lambert, when he was here pointed out that in effect when dealing with automobile insurance as did Mr. Addison, that the risks were rated and in fact the same insurance company, just looking at automobile insurance, divides the drivers up into different classes under 25, over 25, female drivers, and so on. Surely if this approach was taken by a central deposit institution any additional amount paid for insurance purposes by the banks would obviously be very limited, unless they were called upon to subsidize the others, and there are very sound objections to that.

Mr. BINHAMMER: Yes; if we are able to calculate risk on a firm basis then, of course, those institutions whose risk experience is very low would have a low premium, particularly if already we do not have to assess them the additional cost of supervision.

The CHAIRMAN: Yes, but you continue to supervise in any event.

Mr. BINHAMMER: Yes.

The CHAIRMAN: Another question; Mr. Lambert has made comment, as have other members, about deposit taking institutions and so on. Have you any suggestions to make to us as to how we might define deposit taking institutions for the purpose of the type of scheme we are looking at this morning?

Mr. BINHAMMER: No, I really do not. I am in a bit of a quandary myself because I see where I would like to have it for trust companies, loan companies, Caisse Populaire, and credit unions. I do not know if we can bring the finance companies in on it. We must do something for the finance companies but I just do not know if they belong in this package.

The CHAIRMAN: Would this not be a matter of definition if you use an approach in which you look at the matter in terms of obligations not coming under control of securities commissions in the provinces or obligations which are short term and almost demand types. Are they not similar to deposits of chartered banks in that sense?

Mr. BINHAMMER: They are. I do not know what the legal status of them are. This would be difficult to define.

The CHAIRMAN: But in a sense that is why I am suggesting it is somewhat similar to the Porter Commission approach.

Mr. BINHAMMER: Yes.

The CHAIRMAN: One final point; you have in your opening statement depreciated to some extent the psychological or advertising effect of being able to say you are a member of the deposit insurance scheme. Yet, and I may have misunderstood your approach, in your brief you seem to look more kindly on the advertising effect. For example, on page 6 you refer to the objections of institutions in the United States which are having to go through schemes. The same type of objections that are brought before us—the fact that they do not need the supervision or they do not need to pay a premium because they are very sound but then you go to say, and I was quite impressed by this when I studied your brief several days ago:

By and large, however, for most institutions these objections have been not as important as the competitive advantage gained by belonging to the F.D.I.C. as the public has grown more and more aware of the protection provided to them by deposit insurance. This same kind of advantage, while not significant for Canadian banks, would be important for “near banks”.

As I say, in your brief you seem to look more kindly obviously on this concept than you have in your supplementary opening statement this morning.

Mr. BINHAMMER: I have done some more work on this and—

The CHAIRMAN: Let us be reasonable. I do not criticize you for doing so but I think that we should have the benefit of your additional thinking.

Mr. BINHAMMER: Yes. I think I have changed my mind somewhat. I feel much more strongly now, as I indicated in my opening statement, that we have to have carrot for the near banks to join on a voluntary basis. I do not think the psychological factor that exists in the United States exists here. I may be wrong.

The CHAIRMAN: What about the conditioning of the attitude of the Canadian public by being exposed to American media, and they see the ads of United States institutions saying that they have deposit insurance and so on? Would this not have an impact on the minds of the Canadian public because they have already seen the advertisements, and so on, in the American media which we all look at so frequently?

Mr. BINHAMMER: I think somebody made the statement here this morning that it may be a disadvantage to some of the institutions because immediately they become suspicious where the public is concerned.

The CHAIRMAN: My one final point is another suggestion. You mentioned the carrot. I remember Mr. Lambert referring to the California approach which says that all the institutions of that state have to belong to the federal scheme as a condition of getting a provincial license. What about the possibility of the federal government suggesting to the provinces that they change their law to say that any provincially chartered institution to get their charter or keep it must belong to the national deposit insurance scheme? I throw this out for your consideration rather than that of the Committee. It came to me while I was listening to the discussion, I must say.

Mr. MORE: Just as an interjection, Mr. Chairman, perhaps Quebec has indicated that that would not be their position, have they not?

The CHAIRMAN: No, that is true. We will have to deal with that and I think you are quite right.

Mr. MORE: We do not know about the provinces.

The CHAIRMAN: Just dealing in general with this matter, do you think this is a useful approach of federal-provincial co-operation.

Mr. BINHAMMER: Yes, it could be. This would be a carrot. This is the point.

The CHAIRMAN: It would be more than a carrot; it would be a provincial obligation to say to the institution which wished to have or to keep their charter, you will not be able to do this unless you join this national scheme, which is a thought, as I say, we might want to think about as we go along. Mr. Cameron.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Dr. Binhammer, I have been struggling with the way in which you have, shall I say, advanced from one carrot to another and apparently have some quite different purposes. I gather that your idea of the value of a deposit insurance scheme is primarily that of bringing these near banks under federal supervision. Is that correct?

Mr. BINHAMMER: Under supervision.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Under supervision. I was struck with your comments on page 11 of your brief regarding the number of home loans, the banking associations, that have required rescue operations on the part of the F.S.L.I.C.

When I was in Washington about three or four weeks ago another of these savings and loan companies went up in smoke. I forget whether it is officially in bankruptcy. At that time there was a lot of pressure for, I think, the Federal Home Loan Bank Board to take over this company because they had been unsuccessful in getting another and stronger institution to merge and take them over. It would appear that the deposit insurance as operated in the United States has not been altogether effective in the protection of the depositors. Do you agree that is the case?

Mr. BINHAMMER: In so far as there have been some failures; yes, this is true.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): And they have had to come to the rescue.

Mr. BINHAMMER: Yes, they prefer to come to the rescue.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would you agree that the inspection aspect of the operations of this corporation are not as effective as they might be?

Mr. BINHAMMER: Let me put it this way. They are not foolproof, unfortunately. I do not know of any inspection or supervision scheme that can be entirely foolproof.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No, except that we have not had a bank failure since 1926, I think it was.

Mr. ELDERKIN: Nineteen hundred and twenty-three.



Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then you produce the other carrot to persuade these institutions to come under federal control, that of a bank of last resort. But then you introduced another idea in connection with this, that this would not merely induce them to come under supervision, but would also be a means of channelling funds into, in particular, housing mortgages which seems to me a totally different idea; that is, the purpose of it. I am wondering what your comment would be on the answers I got from the Governor of the Bank of Canada on this aspect of our problem in Canada when I asked him if there was any way he could see in which we could by the use, manipulation, perhaps of the interest rate, channel funds into desirable social objectives such as housing. Mr. Rasminsky was very definite on this that there was no way of doing this except by fiscal measures; in other words, by the government getting into its hands sufficient funds to make public investments. I wonder what your comment would be on that in light of your suggestion that by establishing this institution, this bank of last resort, we might overcome this problem of funds not going into these desirable areas which presumably are not as profitable as other areas in the economy.

Mr. BINHAMMER: Well, I wholeheartedly agree with Mr. Rasminsky that it is not its purpose of the Bank of Canada as such to allocate funds to any particular sector of the economy.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): That was not my question. My question was whether the level of interest rates could be manipulated, shall we say, using it not in a pejorative sense, in such a way as to encourage the flow of funds into these areas. He seemed to think that there was no way of doing it.

Mr. BINHAMMER: Let us assume that the institution I have in mind wants to encourage residential home construction at a time that the near banks have difficulty in attracting sufficient funds from the public for this purpose. At such a time this institution which I have in mind could discount mortgages or the securities that the near banks hold at an advantage to the near banks and in this way could provide funds to the near banks to extend their lending activities. Again it would use the interest rate to attract the near banks to come to it for funds.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I should say I am glad to hear you say so.

The CHAIRMAN: Mr. Cameron, if I may interrupt at this point. It is our usual adjournment time and I think we should inquire whether you or other members have further questions for Dr. Binhammer. If so, we can continue this afternoon before calling on Dr. Slater, our next witness who is with us. If not, we can excuse Dr. Binhammer at this stage. What is the consensus of the Committee?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I have no more questions.

The CHAIRMAN: First I want to make another comment in response to Mr. More's very useful point about the California approach and I just thought of a way, if I may suggest it to the Committee, of getting around the problem of one province not joining, and that is this. To do business in any province you need an extraprovincial licence; therefore, if all the provinces except one join they could in effect, each of them, say to the institution from the other province, you cannot do business in our province unless you join the federal scheme. I just throw that out for further consideration.

I also want to thank on behalf of the Committee Dr. Binhammer for his very stimulating and provocative brief and the discussion we have had. I think it will help us quite a bit when we are in a position to study the government's definite legislative proposals on deposit insurance.

This meeting is recessed until 3.45 p.m.

#### AFTERNOON SESSION

The CHAIRMAN: Now, gentlemen, I would like to resume the meeting. Our witness this afternoon is Dr. David W. Slater, Professor of Economics.

Mr. ADDISON: Mr. Chairman, may I raise the point that because of the discussions with the Mercantile Bank perhaps Mr. James Stillman Rockefeller might communicate with Mr. MacFadden that he will accompany Mr. MacFadden when the Mercantile Bank appears after the Christmas recess.

The CHAIRMAN: Mr. Lambert.

Mr. LAMBERT: Well, my suggestion is that perhaps the steering committee could take that under advisement at its next meeting.

The CHAIRMAN: Yes, I think that is a proper approach.

An hon. MEMBER: Shall the motion carry?

Mr. LAMBERT: No, I am not making a motion I am just—

The CHAIRMAN: You are suggesting to me as chairman, and through me to the steering committee, that this be communicated.

Mr. LAMBERT: Yes.

The CHAIRMAN: That is right. I might say that it is my understanding that it was the intention of Mr. MacFadden to be accompanied by the individual in question, but we did not go into this further because he will not be appearing in any event until the new year. Your suggestion has been noted, and there will be a report back to the committee.

Now our witness this afternoon is Dr. David W. Slater, Professor of Economics at Queens University. He received his degree of Bachelor of Commerce at Manitoba, Honours Bachelor of Arts degree at Queens and his Doctorate at Chicago, and his speciality is international trade and money and banking. I would ask Dr. Slater to present his brief in summary fashion, in the same manner we have been using up until now, and after he does so we will proceed to questioning. I might say to the committee that actually Dr. Slater is presenting to us his original brief and a further brief which he has prepared in the light of the legislation actually referred to us. The original brief was a table based on the original bill. I would suggest before calling upon Dr. Slater that, following our usual practice, we deal with the matter by first discussing the specific topics raised by the briefs and then general matters. May I also suggest to the Committee that we consider both briefs together following this order. I will suggest the order right now. First, the question of the definition of banking and federal control of banking which Dr. Slater discusses on pages 1 to 6 of his brief. Second, the question of deposit insurance which Dr. Slater discusses on pages 6 and 7 of his brief. Third, the matter of interest rates which is discussed on page 7

of his second brief and also in his old brief, and there are some matters in the original brief which would continue to be relevant even though one of his major points has been dealt with by the second bill which we are actually considering. Then as the next topic I suggest we discuss the question of charges for inter branch collection, again raised by both of the briefs, followed by Professor Slater's views on the question of broadening the clearing house system. Then, Dr. Slater touches briefly on two issues in his original brief; the question of control by Canadian banks of other institutions and the question of foreign ownership of banks. Finally, in the old brief he has touched briefly on mortgage lending and reserve ratios.

I suggest we call this a melding of the two documents which, I think, will permit an orderly discussion of the principal points which our witness this afternoon is intending to raise with us. Have I analysed the two briefs in a reasonably concise manner, doctor?

Mr. SLATER: In an admirable fashion, sir.

The CHAIRMAN: Thank you. I hope what you said is on the record.

Now, doctor, I am sorry for this further interruption but I will again invite you to present your brief.

Mr. SLATER: Mr. Chairman, it is a great pleasure for me to appear before your Committee and I will try and be of some minor help in your deliberations. It may well be the habit of people when they appear before you to establish their bona fides. I think it is proper for me to say that I am a debtor of a Canadian bank, which I think probably establishes the proper bona fides for this committee.

The CHAIRMAN: We are all members of the same club, in one way or another, I suppose.

Mr. SLATER: I would like to speak briefly to the matters raised in the brief of October 31, which deals specifically with Bill C-222 which is before you, and very briefly with one or two things raised in an earlier brief which was put in in response to the older bill, certain parts of which have, at least, become redundant, and perhaps leave until your questioning many of the matters that were raised in the older brief.

Now, dealing first with the question of the definition of banks, I think it is fair for us to keep in mind when we begin how inherently difficult and complicated is the subject of the constitutional matters with respect to banking in this country. I think it is also very important as we start into the subject for a person like myself to remember—you people, I think, remember it all the time—that there are many considerations you have to take into account in designing your legislation and your approaches to regulation. I have taken the view that it is attractive for us to attempt to sort out a definition of banking and to think about the federal responsibilities on this matter even though the type of solution that is embodied in the legislation may very well involve a whole variety of co-operative schemes and a whole variety of approaches of putting things together, co-operative schemes with other governments, and so on.

I have taken the position that we should at least attempt to sort out the matter of the definition of banking and the federal constitutional responsibilities.



I begin from the point that there is, in the Canadian constitution, a clear and definite responsibility on the federal government to concern itself with banking in Canada, currency in Canada, coinage in Canada and similar sorts of things. The question to which we have to address ourselves is what are to be the bounds on that responsibility? I began with noting that banks, like other financial institutions in this country, are multi-functional. We have in a certain sense in many of our financial institutions a kind of department store of finance approach, and as our banks are multi-functional it means, of course, that defining their functions is a rather complicated affair.

It seems to me, however, that out of all of the functions and characteristics of banks there are two which are the fundamental or primary basis for purposes of the Bank Act. That is to say, there are two considerations that underlie banks and money being singled out for special or different treatment than, let us say, trust companies in their ordinary trust functions or manufacturing companies in their operations. The definition of banking for your purpose, it seems to me, is a matter of what are those primary functions that underpin the selection of banks for this special constitutional treatment.

Now, two points put together seem to me to be the fundamentals here, the first of which is that the crown, the government of Canada, inherently must be concerned with the quality and nature of the items which make up the money and currency of a country. It is simply no good at all in any kind of modern complex economy if we have to look at the particular kinds of instruments that are part of our media of exchange and ask which ones are good and which ones are bad, and which ones are better and which ones are worse. You cannot run a complicated modern economy with that kind of mixed bag of money and currency. The sovereign has to be concerned with the quality of the country's money. Closely related to that, the national government is the only government that can discharge the responsibility of managing a nation's money in an international setting. This is a closely related reason for money, and those things that constitute money in a community, being picked out for special attention.

The second reason is that the government of Canada must have some concern for the amount of money, or the amount of things that are the moneys and near moneys of the country, that those sorts of financial claims require special attention because they have a special significance for the general state of the economy—its growth, its stability, all of these sorts of things. It is certainly not so that the quantity of money is the root of all evil or the secret of all success in these matters, but it is still true, even with the most modern sorts of views about money and monetary institutions, that the kinds of financial claims, which are your money and your very extremely close substitutes for your money, the amount of those things are of special concern to a nation and therefore to the national government and they are embodied, therefore, in a constitutional position.

The next stage of the argument is to then try and pick out what things, in a sense, have this special money characteristic, and the thing we must note is that these things which have this money characteristic have so very largely, at any point of time, by virtue of custom or the attitudes and practices of a people. It is simply not so that the bulk of the things which are the money get that characteristic because they are given a legal tender characteristic. Historically, at the time of Confederation, in Canada, the most important element of our money in

Canada was the banknotes, which were the debt obligations of our banks, and to some extent—it is not the whole story—the reason why the Bank Act had special attention paid to it at the time of the British North America Act was that the bank debts were, in fact, principal elements of the money supply of the country. If any sovereign had to be concerned with the quality and quantity of money in Canada, it had to be concerned with banks. I think it is fairly clear nowadays that there are certain things which are prime elements in our money supply; our currency, Bank of Canada notes and bank deposits which are subject to cheque. These things are clearly treated by us as money; these are the things which are our media of exchange; these are the things which have wider general acceptability among us, and nobody would argue nowadays about the role of a Bank Act or a government concerning itself with bank deposits subject to cheque.

The question then arises about what other things have the characteristic of being fairly widely or fairly generally used as being a media of exchange and in practice entering into our payments mechanism in Canada. I do not think we would have very much argument any more that the chequeable elements of the deposits of trust and loan companies are certainly extremely close substitutes for the chequeable elements of bank deposit accounts and, in fact, there is really not much to pick and choose between them. As one moves down the line there are some additional financial claims which are, in fact, used in the payments mechanism, which are near moneys, and many of these have taken on the character of being nearer moneys, better substitutes, et cetera, than they used to be.

I think it follows from this that if institutions perform the function of supplying instruments which are part of the money system of a country, and if the institution does the things that are necessary to facilitate that, and if the institution in practice makes it comparatively easy and inexpensive to use these things as part of the payments mechanism, then those institutions to that extent are engaged in the business of what we would call banking, or they are carrying out a set of banking functions that are of special concern to us from the point of view of the responsibility of the manager of the nation's money. It seems to me it does not really matter what government created an institution in the first place. If any institution, having been created, opt into a set of functions, it does not have to take on that set of functions. It must actively co-operate, if it is going to carry out that set of functions, and if it gets into this position then it is in fact carrying out functions of the kind that are the basis for the special attention that is embodied in banking acts. It seems to me that from this it follows in logic but one may have to temper one's logic a great deal with practicality, considering all the other things which one has to consider—that the federal government in discharging its constitutional responsibilities for banking control—the special things that give rise to this special constitutional position—in effect has to draw the line some place and say that any institution which carries out that set of functions is, in fact, engaged in an activity which is banking for the purpose for which we have a Bank Act and for which we have the related acts.

This, it seems to me, is the essential logic of the position. There is a question as to whether one, in a sense, lets the courts somehow take the initiative or forces the courts into a position in which they take the initiative in carrying out this definition or whether the legislature takes an initiative and, in effect, allows its legislation to be challenged or, in fact, on the basis of the legislation proceeds to challenge certain activities on the basis of that legislation. My own view on



the matter, and on this I will have to defer very much to the constitutional lawyers—my expertness extends to politics, too, at Queen's University and not much beyond that—my view on this, therefore, as a lowly amateur, is that in principle at least a definition in the legislation is a legislative responsibility and that, of course, the courts will come in in the matters of testing, et cetera, either on the initiative of somebody other than the government or on the initiative of the government, as the cases arise. It seems to me not really very appropriate for the matters of definition to, in a sense, be rolled over and pretty nearly completely put on to our courts.

The next step, of course, is to say, well, that is the logic of the argument and one can take it apart. The next question which arises is where do you draw the dividing line as to what is banking and what is not banking, because certainly if you are going to produce any definition it has to be a definition that is fairly clear. It can be rough and ready, it does not have to be perfect, but it has to be fairly clear and definite. The second issue is even if you accept this idea of a definition in principle, do you have it as a position from which you start in and say that this is our responsibility? Of course, banks do many things other than the things we are talking about. Maybe we, in fact, work out a variety of means by which we exercise this responsibility, and many of the things that are in fact, worked out are worked out by co-operative devices, including the implications of a deposit insurance system and other possibilities.

As to the definition of claims and where you draw the line, you all know the Porter Commission tried its hand at this, defining things essentially in terms of any institution which was issuing short term debt and particularly short term debt of a kind that enters in a significant way into the payments mechanism to the extent that it issues those things, it is a bank or it is engaged in a banking type activity, and then your regulations will be made on that basis. It seems to me that the things that are very clear are that you can say anybody who is engaged—you have to look below the surface for the facts of the situation—in the business of taking deposits which are, in fact, redeemable on demand or transferrable by cheque is engaged in banking, and that is one fact that is pretty easy to establish. If you want to go beyond that—and there is a pretty good case for attempting to go beyond that—to see if you cannot mark out some other sets of things where you have things which are, in fact, relatively close, extremely close substitutes, things which, in fact, enter significantly into the payments mechanism, and see if you can mark those out and draw your dividing line to include those, the Porter Commission suggests a particular route.

As to the approach to regulation—I think my position is very simple on this one—it is that I can see that many considerations may lead you to the view that various inter governmental cooperative schemes might be used in the discharge of the federal responsibility with respect to the banking functions, but one must remember that many of these institutions that carry out some banking functions carry out a lot of other functions too. They are all kind of tangled up with one another, and some of those other functions are, in fact, things which clearly are in the jurisdiction of other people or have a basis for regulation which is different than these particular banking functions. So, one may, in a sense, have to put together a sort of package deal which does this with respect to the banking things—the things which have to be done—in ways that you can do the other things and link them together. Therefore, it does not necessarily follow from the



logic of one's definition that one comes in in a rather bloody-minded way and says, that anybody who is in the banking business in any way, shape or form has to do this and this and this, that is the only thing for it, and everybody else has to get out of the business. I think there is a lot of flexibility that could be worked out here.

Now, I will say a very brief word about two or three other things. The next thing on the list and in the brief is the matter of the deposit insurance. In a way, I think it is my understanding that the deposit insurance proposal is that this is essentially a vehicle in a tactic of co-operative approach to banking and related financial legislation. It is essentially a tactical approach. One hopes that out of the deposit insurance one will, in fact, make an instrument which, by various schemes of—to use the language of this morning—sticks and carrots, can be used to improve the banking situation in this country.

This, of course, really raises a number of questions. The first question is that it might be that in applying the deposit insurance one will have to decide who qualifies for what grade of insurance and on what terms. There is no inherent reason why there cannot be some sort of flexibility here but I think one should be fair about this. There is a great deal to be said for a single package deal when it is regarded as an instrument in a total development. In the brief, however, about the deposit insurance, I took the view that since the deposit insurance is a vehicle, the important thing is to look behind it. The obvious things are that deposit insurance will not do a job unless you have regulation and supervision. It can, of course, be co-operative regulation and supervision, but you have to have it. Deposit insurance will not do a job unless, in fact, trouble is detected and corrected before institutions get into really serious trouble and, finally, deposit insurance is not enough. You cannot get the absolutely fundamental underpinning that you need for your banking institutions and banking functions unless, in fact, in addition your institutions have access, directly or indirectly, to the central bank's lender of last resort facilities and other sorts of facilities. Deposit insurance, even if in itself it is done terribly well, it is not enough to do the job with which you have to concern yourselves.

Regarding the way in which deposit insurance might be used as a vehicle, Professor Binhammer this morning suggested a way in which one might couple the deposit insurance function with some other functions in a way to make a meaningful package. It seems to me, as I see deposit insurance working out, the biggest stick that is probably involved, and I cannot really believe that this is a problem for most provinces, is that the provincial governments, I think, have to take the initiative to, in fact, put or persuade, or do whatever it has to do, to get most of its institutions which are engaged in banking type activities into the deposit insurance system. There are lots of ways the provinces can do this, but it seems to me that no province in this country can be very happy nowadays with the prospect of some of the—to use the popular term—near banks, which are creatures of its incorporation laws, getting into the kind of trouble that we have had in the last while. It seems to me, rather, that provinces must generally be looking for sensible means by which they can, in fact, get the institutions which are chartered by them put into a stronger position.

It is perfectly clear that the proposals that have been talked about, particularly if you have a scheme by which deposit insurance covers the banks and the other institutions, and even if there is a kind of dividing up into two classes for rates, and so on, it is likely there is going to be an element of subsidization by

which the weaker institutions are going to be subsidized to some extent by the stronger institutions. That seems to me to be a fact of life. It is not to be sneered at in itself. It is not a decisive consideration because it seems to me that in looking at the legislation one must look at the thing as a whole.

Deposit insurance can have associated with it a scheme of lender of last resort or discount window facilities directly or indirectly for the near banking institutions. There is a possibility of improved access to clearing systems, there is improved information that would help them in their operations, and so on. It seems to me there is a whole series of package arrangements which could be put together to make a deposit insurance system work.

The last thing I will say a word about here is the matter of interest ceilings. I am pretty much on the record rather clearly about interest ceilings and therefore I can be very brief. I strongly support the recommendations of the act that the ceilings be at least lifted. It seems to me that the existing ceilings are really ineffective, they do not do the job that ceilings might, under the best of circumstances, be designed to do. I can see in the abstract some merit in systems of selective ceilings by which all bank business gets dropped into three broad categories, or something like that, and there is a ceiling system that is roughly appropriate for each of these. I realize that that is a very difficult thing to work out, and I do not know enough about the problems of working it out to have much confidence in it. But one thing that is absolutely certain is that if you set the ceilings on bank lending rates too tightly nowadays, you end up by not doing the job that you intend by your ceilings, because the starting point is that the premise in this country is that our banks are department stores of banking. They are there to carry out a multitude of functions. If you are going to have the banks carrying out a multitude of functions, they are going to have to carry out functions which differ a good deal in costs of administration, in risks and some differentiation in the terms on which lending is done, and this has to be a part of any effective and equitable banking system which carries out a broad range of functions. The present tightness of ceiling that has existed in the last couple of years has been far too great; it has been breached over and over again; it has driven the banks to all kinds of devices to try and get around it; it has encouraged the development of banking satellites, which I think is a retrograde step in general; it has introduced distortions involving lending; it has been ineffective; in fact, it has not protected the particular income groups, and so on and so on, that it was intended to protect. Indeed, I think I can make a pretty good argument that the effect of the ceiling has been to make borrowing more expensive for the people that you are in fact interested in protecting. Therefore it seems to me there is no question at all about the desirability of raising the ceiling from its present position. As for the ultimate removal, I think all of us recognize that we are moving into a realm in which there is a belief that competition which is actively promoted by government action will, in fact, be the principal protector of the public and I think—as I said in my brief—it is a little too soon to be absolutely sure of this, but I think it seems to me to be one of the general lines where we should have an attempt at development.

The CHAIRMAN: I think we should give you a bit of a rest, Dr. Slater. You have been giving a very useful extrapolation on your very interesting brief, and perhaps if you have any other introductory comments on the other topics we can come to them when we get to those areas specifically. I recognize Mr. Fulton first.

May I suggest to the Committee that although I originally suggested we deal first with the topic of definition of banking and federal control and then deposit insurance, it is obvious, to me at least, that they are so inter-related that perhaps we should really consider them together rather than separately. I would make this suggestion to the Committee. Mr. Fulton, you may proceed.

Mr. FULTON: Thank you, Mr. Chairman. Professor Slater, I would like to say at the outset that I find myself certainly in principle, in agreement with your approach that it is desirable to define banking to achieve a number of objects; clarity of legislation, drawing under the excellent federal control and inspection system institutions engaged in the broad sense in the banking business, and so on. I take it that these two are among the more desirable effects that you would attribute to a definition of banking; clarity and drawing under one general umbrella of control and inspection institutions generally engaged in that business?

Mr. SLATER: Mr. Fulton, I think I have attempted to take the position that the definition of banking would contribute in this direction. I do not think that in itself it will produce what one is interested in producing, but it does seem to me that it would have the merit of underlining the nature and the fundamental premise of federal responsibility, a premise that might very well not necessarily be always worked out as a federal inspection operation but would at least be the federal government's starting point in any negotiated co-operative scheme.

Mr. FULTON: I ask this next question purely for information and not in any attempt to be snide or facetious. So far as I have looked at it, technically it defeats me and I am going to ask you whether you have had more success. Have you tried your hand at such a definition of banking? I made the premise that I agree with you in your approach, and I was wondering whether you could help us?

Mr. SLATER: I think the position that I would take on this is a little eclectic in the sense that Richard Sayers, who was the mastermind of the Radcliffe Committee report in the United Kingdom, put it: We are not dealing with an area that is inherently amenable to extremely sharp dividing lines by which you say everything on this side is money and everything on that side is not money. Everything on this side is banking in so far as we are defining banking in terms of certain characteristics in creating money. I think what I would say is that there are certain distances we can go in drawing this dividing line in which, it seems to me, we can have nearly universal agreement at a particular point of time. That is, at the present time we can get nearly universal agreement that any institution that is—and to the extent that it is—engaged in borrowing under demand deposit accounts or checkable accounts is, in fact, engaged in a banking activity. On that you have to be very clear about it that you have to take the thing as it exists, not as it appears on the surface. That is, there are institutions which enter, and have entered in the last few years, in this country into borrowing contracts in which they have borrowed for what appeared to be a fixed term but, in fact, they operated in such a way that you could turn that piece of paper over for practically no transaction cost, you had no risk about your ability to do this, and you could do it at a kind of market adjusted rate that was clear and definite and you knew the terms under which this was going to happen. There you have a kind of claim which is formally not checkable, and on



would say that that is something which is not money, but if in fact there is a fairly widespread practice of turning these things over in these terms and if institutions acquiesce, and not only acquiesce but, in fact, actively engage in that kind of activity then, of course, our definition could be extended to include those things. I only once in my life sat on a large chunk of trust funds for a number of months and I employed them, in fact, in deposit certificates and in trust companies. I was uncertain as to how quickly I would need some of the funds. I was told, and told in very straight-forward terms, that if I needed to turn this thing over more quickly that it was perfectly straightforward for me to do so. Now, when one moves out from chequeable deposits, or things which are pretty actively and clearly used in the payments mechanism, beyond that stage, then life gets a little bit more difficult. The problem here at any given time is essentially one of what is central practice of a community? Practices change. You and I could agree pretty readily that trust company deposit certificates, if they are in fact used as regular part of a payments' mechanism, probably ought to be included. The same thing applies to bank deposit certificates. Now, if you move out to other sorts of claims it is more difficult, and I think I would be inclined to suggest you draw the dividing line of the claims you are especially interested in about as far out as you can do it clearly at any given period of time. In fact if there is a practice actually in use in the community of some size, some persistence, some significance, draw it there. If you come back at it ten years later—and, of course, things are going to change and you will have to draw it differently then—you do recognize the inherent customary nature of this sort of thing and the fact that customers are themselves changing and emerging.

Now, there have been various attempts to lend additional precision to this. The great difficulty in this again is the problem of the part versus the whole. In the United Kingdom there is a controversy as to whether post office savings deposits should be included in the money supply. Well, the point there is that if you want to make a payment you go to the post office savings bank, you make a withdrawal or get a money order and, in fact, they are even developing a gyro system in this; you go to your post office savings bank, and you use the gyro to make payments at a distance. Well, the fact is that in England the custom of many people, when they have excess money, is to put it into the post office savings bank. They perform a whole series of activities in the post office savings bank account, in institutions where they buy their sweets, where they buy their stamps, so that they are going in and out of these places in a routine way. Well, in that situation I think I would say that the post office savings banks accounts are used to put money in and to pull money out. They are, in fact, used as a continuous part of the payments mechanism in the U.K., and if they amounted to anything of any significance you would draw your definition to include them. I think this is the best I can do, sir.

Mr. FULTON: Thank you. I wonder if I could now leave that. I realize that perhaps I should have left it until the end. I would like to go on from there. Now, having stated clearly that I agree with the definition approach, may I for a moment be the devil's advocate and try to explore the difficulties.

I would like to put this question to you. If we were to define banking specifically in legislation, and you have to have limits, when you are a legislator you have to be at least clear and definite, might it not be more difficult to exercise effectively any jurisdiction and control over non-deposit institutions? I

will elaborate in this way. If, for the sake of argument, you might agree with me that a deposit-taking and lending institution is clearly a bank, this umbrella might, therefore, include trust companies to the extent that they indulge in that business so they would presumably be covered. However, what about finance companies which do not take deposits? What I am getting at is that if we assume that your umbrella has been sufficiently clearly extended to include what are commonly called near banks, then might it not be more difficult to bring under the umbrella the finance companies, which are not within the definition, and to exercise any control over them. In other words, is this a danger of attempting definition?

Mr. SLATER: I do not know the answer to that question, Mr. Fulton. A government's interests and activities influence institutions, as it were, indirectly rather than directly, and certainly to the extent that the institutions that are in your net of banking are competitors, as borrowers and lenders, with institutions that are not in your net. That is certainly the situation nowadays. In some respects at least the federal government's activities, with respect to the matters that are directly under its responsibility, spill over through the competitive channels. This is certainly true to some extent with respect to the effectiveness of monetary policy, and inasmuch as people are able to compare many of the terms and conditions under which, let us say, they could lend to a bank versus the terms and conditions under which they could lend to other people, there need not be a conflict.

Mr. FULTON: May I put it this way. I would admit that they will be influenced by federal activities, even outside the umbrella, but I am concerned now with inspection and control because, like all other members and the public generally, we are concerned with recent events where companies have gone belly up. I am thinking of the direct control.

Mr. SLATER: My feeling on that, I suppose, is that it really turns on questions of example and response of the other interested governments and the demands that depositors place on institutions. I would think that in the present environment institutions which were not in a significant way in the banking business but were in other kinds of financial business in relationship to the public, and with some element of a trustee position, that many of these would at least have to try and indicate that they, in fact, were good fellows, they were of good quality, but I cannot be certain of this.

Mr. FULTON: For purposes of elaboration or, at least, of forming a basis for my further question or questions, would you agree that I am stating it correctly if I say that finance companies,—take Industrial Acceptance Corporation as an example, that is what I mean at the moment by finance companies,—exert quite a considerable influence on the credit system and purchasing power in the country by their activities and that if we are dealing with monetary policy in its broad sense, the activities of finance companies are a significant factor in that field?

Mr. SLATER: I think the position is that they are significant factors—and this is a very difficult area indeed—and I think it is possible even if there are certain kinds of improvements in their competitive position due to, let us say, something about their technology or organization, that that in itself can have an over-all effect on credit conditions in the country. On the other hand, my impression is

that these companies, and particularly those which are actively and continuously having to raise funds in the capital market—as Industrial Finance, Traders Finance, and so on, would be doing—that many of these are rather substantially influenced, indirectly, by the general governmental activities with respect to credit conditions.

Mr. FULTON: Per contra, they also have a fairly substantial influence in the credit field.

Mr. SLATER: This is quite right. Now, there is the question of the influence which in a sense is a kind of ongoing sort of reaction in which, like any other kind of institution, there is the other question which has exercised many people, which is the question of whether the development of these institutions, their growth, their freedom to manoeuvre in relation to the other institutions, has in fact fundamentally undermined the ability of a government to carry on its financial policies.

My impression is that the evidence supporting the view of large and fundamental undermining is generally not accepted by the cost economists that I know.

Mr. FULTON: Well, we will not get into an argument. Your opinion, I think, coincides pretty generally with mine in that the statement I made earlier and put to you then, generally speaking you agreed, they are significant. If we are talking about the control of monetary policy, including the availability of credit, and so on, that they are a significant factor.

Mr. SLATER: Yes. What policy conclusions you draw from that, of course, is another matter.

Mr. FULTON: Yes.

Mr. SLATER: That is right.

Mr. FULTON: Then I come to this question. Given the possibility that it is difficult to define successfully or, alternatively, assuming that no definition of banking will be undertaken, do you favour alternative devices such as deposit insurance to attract related institutions under the umbrella of inspection and control?

Mr. SLATER: I think I would take the position, Mr. Fulton, that one has to face the facts of life in the financial systems as they have emerged at this stage and not only in Canadian development. What we are dealing with is something that has emerged nearly every place that you can go in the world in a developed area. I think I would certainly support the view that we must, by some devices—deposit insurance, co-operative arrangements between government, and such like—face up to the problems of improving our financial system to protect the public, to improve its efficiency, and these certainly are not the most important things for us to do, but these are quite important and significant things for us to do. My own view is that one can get quite a long way, probably, by a variety of informal devices.

Mr. FULTON: I have just one more question, Mr. Chairman. Would you agree with me that the device of deposit insurance is most readily applicable to that kind of financial institution which takes deposits?

Mr. SLATER: Yes.



Mr. FULTON: But not readily applicable to institutions that do not, such as straight finance and lending companies, which take over a contract of purchase from the vendor and in effect it is counted with them, and then the finance company collects from the purchaser. This would not be a deposit transaction and therefore that kind of company is not readily amenable or tractable by the device of deposit insurance.

Mr. SLATER: Well, I think the position would be this. I think one perhaps could almost make a distinction between wholesale depositing and retail depositing. That is to say, whatever the name of the company, if in fact it engages to a considerable degree in borrowing from primary lenders, and particularly if it borrows in forms that in a sense enter into the payments mechanism pretty actively in the community, then no matter what its name, it is in fact engaged in a deposit kind of business and presumably the net of deposit insurance could be extended to that. Prudential, presumably, is a case in point. Now, to the extent, however—and this would be the situation for Industrial Acceptance, and such like—that they are primarily borrowing on the market large chunks of funds, and that is the source of their financing—they may sell things to primary lenders, but the primary lenders are your corporation treasurers who lend in large blocks, and so on—but that type of thing is not a deposit type business and presumably would not be the object of one's deposit insurance route, and I think it is not very amenable to being handling in that form.

Mr. FULTON: Then would you agree that that type of institution—large or small—might be amenable or tractable under an umbrella by a device such as having extended to it the benefit of a lender of last resort? This would be a third device. You have the device of direct control over chartered banks, you may have the device of deposit insurance for the deposit-taking institutions, and the third device of lender of last resort to draw in the third type of institutions.

Mr. SLATER: One must remember that there are all kinds of things one is trying to do by a lender of last resort function. In the ultimate extreme you are trying to put in place a device that will permit you to go through economic adjustments and changes without these horrendous crises in your financial system; that is the ultimate thing.

Mr. FULTON: I, at least, would have in mind the objective of enabling the government, if you like, or the control system, to exercise some control and inspection; that is an objective of the device as well, and in my mind an important objective of the device.

Mr. SLATER: I think the following is what is right. Any organization which, directly or indirectly, has a lender of last resort position in effect has access to emergency supplies of cash. Usually there are two elements involved. One is that the institution puts up some sorts of claims that if it had to sell off it would have to sell off at fire sale prices, and that does not make any sense the other thing is that there has to be an element of discretion by the lender of last resort that this is a genuine emergency and that people, for reasons that are beyond their control or influence, find themselves in trouble, as in situations of bank runs and banks although they have been perfectly well managed, find themselves in trouble. It is a combination of the assets and, in a sense, this understanding and appreciation, the confidence between the lender and the borrower, and this is vital.

Mr. FULTON: Would it not be perfectly consistent and, indeed, only sensible as a condition to having an institution standing there available as a lender of last resort to require that that institution be entitled to exercise some inspection and control activity over the other institutions behind which it is prepared to stand as a lender of last resort?

Mr. SLATER: There clearly has to be some basis of confidence there. To be specific, I do not know where one draws the dividing line for inspection or not. In our present arrangement a selected group of investment dealers have lender of last resort facilities as part of our money market organization, but the Inspector General of Banks does not go off and inspect them, you see. On the other hand, they have a limited lender of last resort facility in which the good name and management of these outfits, together with the particular kinds of claims that could be used as security, puts the principle of the lender of last resort thing together on an adequate basis for this purpose. So, I do not think it follows that the lender of last resort facility always necessarily implies a wide-ranging inspection activity. It clearly depends to a degree on confidence, which is something more than simply the pieces of paper that are traded around.

Mr. FULTON: Would it not then be likely to produce a situation where, short of clever and undetectable crime and fraud, there would be greater solidity and stability in the field of the third type of institution I am talking about, perhaps not by direct and detailed inspection and control, but at least by an atmosphere?

Mr. SLATER: I would think that very often the access to lender of last resort facility has accompanying it a kind of special—I use the word loosely—trustee position, and with the privilege goes a kind of responsibility. It may very well have these effects, but I am afraid I simply do not know enough about this to be certain of it, Mr. Fulton.

Mr. FULTON: Mr. Chairman, I appreciate that I have been overtime, so I will defer now.

Mr. CLERMONT: I do not think the translation is operating, Mr. Chairman. It works from the French to English, I think.

*(Translation)*

The VICE-CHAIRMAN: Go ahead, Mr. Clermont.

Mr. CLERMONT: Mr. Chairman, Mr. Slater on item 4 of his brief says that the Parliament of Canada is empowered to define banking activities, that is to define a bank. Could Mr. Slater say if he would accept the definition of a banking institution given by the Porter Commission: it says that a bank is any institution which receives demand deposits or term deposits maturing in less than 100 days or which issues security maturing less than 100 days?

*(English)*

Mr. SLATER: Mr. Clermont, I would be inclined to say that the Porter Royal Commission definition was offered, and I think it should be regarded, as a helpful starting point in this definition. It is based upon a view that at this stage of development in Canada claims which, at the time of issue, had more than 100 days to maturity are not used in any significant way as part of the payments mechanism. There is some use of things that have more than this 100 day

maturity, but it is very limited, and one is not really going to be missing anything that matters very much if you do not include things which have more than 100 days to maturity.

Secondly, I think it is an attempt to provide a simple and a definite rule which is kind of rough and ready but is in some important respects, as it were, in keeping with the situation as it has emerged in North America at this stage of development. I think that one might cut back a little in the number of days that are used for this purpose. You would leave out some things that have in fact been used as part of a payments mechanism, but I do not think if you were to cut it back a little in terms of number of days you would leave out anything that would make that much difference.

The question that is much more difficult, Mr. Clermont, is to see whether one can introduce one or two additional criteria that will, on the one hand, leave out some things that clearly should be left out they play such as small role in the payments mechanisms as to be insignificant and, on the other hand, find some additional criteria as to what things you would put in. When you get into this admittedly the problem is very difficult because you are, in fact, having to embody in legislation things which are, in fact, a function of the customs and the habits in institutional developments in a country at a particular point in time. Certain kinds of claims that have, let us say, 30 days to maturity at the time they are issued clearly are never used in the payments mechanism. Others are used a great deal. I think that what one should probably do here is to rule out a whole series of things explicitly. That is pretty easy to do. You simply say, "Those things are not" and you could name them and that is that, and then to attempt to find one or two additional criteria that will help you to delineate within this. My feeling is that whether you do this sort of thing explicitly, as the Porter Commission did, or whether you do it implicitly and therefore, in a sense, embody your legislation on a recognition of implicitly of the things in fact that have emerged in our society, you can make a choice between the implicit and the explicit treatment of the subject, but that is quite a different choice from the question whether you try it at all. That is the best I can do on the first round at it.

I have taken the position in my brief that I believe it should be tried. It is worth doing, though I recognize that there are many factors, other than economic and other than financial involved in this, which may lead you—having tried the thing—to take somewhat tentative and somewhat flexible approaches to how you in fact implement the arrangements to deal with the banking problems.

*(Translation)*

Mr. CLERMONT: Mr. Slater, would you feel that Credit Unions and Caisses Populaires could be classed as banking institutions?

*(English)*

Mr. SLATER: I think one probably has to make some distinction here between the *caisse populaire* on the one hand and the credit unions on the other, and within *caisse populaire*, probably one has to make some distinction between those which are urban based in the larger urban centres and those which are rural and parish based. My impression—and it is a limited impression that is based on grossly incomplete information—is that the urban *caisse populaire* in



Montreal or Quebec is engaged, as an essentially commercial enterprise, in a range of borrowing and lending business that is of the sort which one would describe in the United States as a savings bank kind of business. That is to say, and my impression is, that some of the activities of the urban *caisse populaire* would technically fall into this definition of banking as I have put it.

My impression is that the rural *caisse populaire* is much more influenced still by the traditional basis on which the *caisse populaire* was developed and I think that the situation there is much less clear. I think the amount of activity that would be in any Caisse, treated as banking activities in this narrow sense, or money creating and money managing activities would be much smaller.

The credit unions, I simply do not have enough experience with. My experience with credit unions in the United States, when I lived there for a time, was that they operated very much like a savings bank, and that for many of them people did not make great use of them in the ordinary operation of their media of exchange or payments operations; that they were used much more in a savings banking role. My impression is that credit unions in Canada are pretty much a mixed bag in this respect at this time, and I am not sure that this makes a huge amount of difference at this stage, whether you get the short term deposit business of the credit unions into a definition of banking or not; subject only to one footnote, and that is that many of these institutions really do require quite a little improvement in their management. There is a good deal of mismanagement; there is a great deal of risk for people in the situations that now exist and some activities to protect the public and improve the operations of credit unions in Canada are desirable, but I am not at all sure that it has to be done as if these institutions were primarily panicky. My feeling is you might run some of their activities under deposit a insurance scheme—

Mr. CLERMONT: Do you think they should get their licences or permits from the provinces?

Mr. SLATER: I concede that this is a very difficult business. Let me put it this way: Many of these provincially chartered and licensed institutions carry on a mixture of activities. They have grown and developed, and the community has treated them as having grown and developed into doing some activities, into doing them on a bigger scale and more efficiently and so on than they used to do. Some of the activities in this mixed bag remain nearly completely provincial responsibility. There is no special federal interest in them whatsoever; there is no national interest in them whatsoever. But at the other extreme, there are some of the activities of many of these institutions which have, in fact, taken on the character of really doing things that are pretty fundamental to the money supply, its quality, the payments mechanism and so on. Whether we like it or not, I think we have a national currency and a national money and with all the things that go with that, and the upshot it seems to me, whether we like it or not, at the moment is that the federal government has a responsibility for dealing with those activities, of any institution, no matter who created the institution, which carries on in a significant way these functions of supplying and participating in facilitating the payments mechanism of the country.

You can leave out the stuff at the margin without losing very much. The point, of course, is that there is quite a lot of the evolution of the activities of institutions other than the banks which is no longer marginal, it cannot be regarded as marginal. I must say, Mr. Clermont, that those are my judgments

and some of my older professors are likely to say to me: "That is all well and good, young man, that is your opinion." I recognize this position.

Mr. CLERMONT: My next question will deal with section 14 of your brief on page 5 where you give us four alternatives:

- (i) to require the institutions other than chartered banks to withdraw from these monetary activities; or
- (ii) to force the institutions engaging in banking activities to obtain a charter under the (federal) Bank Act; or
- (iii) to develop some system

And so on.

If such an institution has received a permit or a licence from a province, how can the federal government interfere in that.

Mr. SLATER: I am very simple minded about this sort of thing and I am really making the distinction between who creates an institution and what functions the institution carries on. Now, this may be a fairly bad constitutional position, but it seems to me that having created an institution is one thing; that institution can choose to carry on a range of activities.

If it takes on a certain range of activities, which by the clear and definite statement of the constitution are national responsibilities, it does not have to take them on, but if it does, if it opts into doing those things, that it takes what goes with that. Now, this is a very simple minded point of view. It does not necessarily follow that one then comes around and starts throwing his weight around in all sorts of silly ways; but, on the other hand, I do not think it is in fact a situation that any provincially created and chartered institution in this country can opt into the business of creating a provincial money, and that is that. It seems to me that is not the state of affairs of the constitution of Canada today. But I simply have to defer to the constitution lawyers here. It seems to me that what is absolutely fundamental here, is to distinguish between who creates an institution and what that institution does and this, as I say, is absolutely fundamental to sorting this out, as I see it.

Mr. FULTON: I think Mr. Slater flatters us. I do not think there are any constitutional lawyers here.

The CHAIRMAN: You, on behalf of your fellow lawyers on the committee here, seem to us to be too modest.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): What I suggest Mr. Chairman is that is for the economist to decide, not lawyers; they are the only ones who can decide what the functions are.

Mr. FULTON: Are there any economists here?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Lawyers outnumber the rest of us.

Mr. FULTON: The next thing you know Mr. Cameron will be asking: Are there any good economists here.

The CHAIRMAN: You sound as if you are trying to develop a special finance committee version of the song, The Twelve Days of Christmas.

Mr. FLEMMING: Mr. Chairman, I think you can take consolation out of the fact that the Good Book says, "out of the mouths of babes come words of wisdom".

The CHAIRMAN: Our witness has described himself as a young economist. He is not that young.

Mr. FULTON: In my question, of course I was referring to members of the committee, not to the witness.

(Translation)

The CHAIRMAN: Any more questions, Mr. Clermont? Have you any more questions to put to the witness?

(English)

Mr. CLERMONT: Parliament during this session has granted two new charters. Do you think the deposit insurance scheme will help these two new banks, if they get a certificate from the Treasury Board, to obtain more deposits from the public, if it is approved by parliament. Will it be easier for these two new banks to get more deposits from the public.

Mr. SLATER: I would think it might make a small marginal difference to a new bank in its operations, but it seems to me that the success of those new banks is going to depend primarily on a whole range of other factors and other considerations. We have a long tradition in this country that even when we had free banking legislation and special charters—there was a day back in our history when we had both—people said, why should we go for a charter under the free banking legislation when we can get a perfectly good charter under this special charter provision. I would have thought that if the new banks were reasonably well managed, and so on, they would very quickly move into a position in which they, in fact, obtained a share of the reserves, a share of the deposit business, and a share of the lending business. I would suspect that there probably will be, in establishing any such bank, a limited period of time when they are building up the confidence of the public and in which a deposit insurance would make some sort of difference to them. I would not expect it to be a really decisive factor with respect to those new banks. It certainly will not hurt them; it will help them a little, I would think, Mr. Clermont.

(Translation)

Mr. CLERMONT: In this way there would be a good deal more competition amongst banking institutions if the new banks could obtain deposits more readily and easily? Was not this the first recommendation of the Porter report, that there be more competition among banking institutions; is that not right?

(English)

Mr. SLATER: This I think, is quite right, Mr. Clermont. The Porter Commission in effect said we had two broad routes that we could take with respect to banking legislation, and we could try to chop up our financial institutions into a series of pieces with limits on the activities of each and special regulations for each, and so on. Or we could in a sense go actively for a system of overlapping competition among our financial institutions, and it seems to me that in general



spirit the new act has taken the position that we, in fact, ought to go for the active promotion of competition among, not only banks, but among banks and other institutions, as a way of improving the financial structure in Canada. I think it is fair to say that Canada is not unique in this respect, but is in fact using the competitive route as the way of improving its banking structure somewhat more aggressively than almost any other place in the world is doing now, as a matter of fact. It seems to me that there are many provisions in the act before you, that are directed to improving the competition among the existing banks and between banks and new institutions and it almost seems to me that the commitment of the Minister is very sympathetic to the view that it should not be all that difficult to charter some additional banks beyond those that in fact have been before you.

Mr. LAFLAMME: Do you think that the deposit insurance then would increase competition among banks?

Mr. SLATER: No. I do not think it can make a particle of difference on the position among banks.

The CHAIRMAN: What about banks and near banks.

Mr. SLATER: Banks, and near banks is another matter. I think it is going to make a difference there. I think we are in a climate, whether we like it or not, in which even pretty good institutions, even institutions with a reputation have been subject to question and one hears a fair amount of even some of the most reputable trust companies having a little bit of the backlash of the events of the last eighteen months. My view is that deposit insurance will in fact improve their position vis-à-vis the banks, that is, the near banks, vis-à-vis the banks.

Mr. LAFLAMME: You do not want to get into the system?

Mr. SLATER: Oh, yes, you are quite right; my premise has been that if you put deposit insurance in place that in fact, you do it with co-operation of provincial governments and a good deal of suasion and a lot of other things that are there to try to make the thing float and that in fact, therefore, you will get deposit insurance in something more than name. The deposit insurance is to be viewed as one instrument in a package, in a tactic by which some of the problems are dealt with.

Mr. LAFLAMME: I think a couple of bankruptcies will help to have these consultations.

Mr. LAMBERT: Has it been suggested that deposit insurance is the fruit juice that disguises the castor oil?

The CHAIRMAN: Order. I think we are being unfair to Mr. Clermont in permitting a supplementary question or two that developed into a full exchange.

Mr. CLERMONT: Had I objected to those supplementary questions, I would have called your attention to it, Mr. Chairman.

The CHAIRMAN: I have—

Mr. CLERMONT: I am not that shy.

The CHAIRMAN: No, but I have some obligation as Chairman to try and make an attempt at least to see the meeting proceeds in an orderly fashion irrespective of objections.

Mr. CLERMONT: Mr. Slater, your brief seems to favour deposit insurance for the near banks but not for the chartered banks.

Mr. SLATER: No, that is not what I have said, I have left myself open to being misinterpreted here. I think there is a lot to be said for the deposit insurance system extending over both the banks and the near banks. It seems to me that the deposit insurance system is fundamentally a vehicle that is to be used to improve our general banking structure in the broad sense of that term. It is probably true that our banks in a sense do not need it but our banks, that is the chartered banks, I think, are, in fact, in a position that they may very well have to participate. They should, in the general public interest, participate in certain things which have an intent of dealing with a broad class of questions which involves them as well as others; and, involves them in ways in which they have a vital interest in the matter of how the other institutions are dealt with. It seems to me that you could say, well this is unfair to the banks to impose on them something they do not need. But my own view is that this should be regarded in the round, in the totality of the things that are done here and, it may very well be a perfectly sensible compromise in the total package of your development to have banks that appear not to need the thing, to participate.

Now it is possible, as your Chairman suggested this morning that you might go for two schedules of rates, that is a possibility to be thought about—perhaps even three schedules of rates. But even that one may be more difficult to work out than it is worth. I think the one thing that is fairly clear is that if you have a deposit insurance system, if you do the other things you have to do to make it work, then the cost of the deposit insurance is in fact not huge.

I have a lot of sympathy for the point of view that Dr. Binhammer put before you that, in fact, there is a good case to me made for perhaps two institutions or one institution for one outfit and none for another or something of this sort. But, my own view is that on the whole I think I see some merit in a single institution perhaps with a differential ratio.

(Translation)

Mr. COMTOIS: A supplementary question, please?

The CHAIRMAN: I must recognize the other speakers before Mr. More and Mr. Comtois. I should say to Mr. Clermont that even allowing for a few extra minutes, his time has expired.

(English)

Mr. MORE (*Regina City*): I just want to ask you this. Do you see merit and anything to be gained in a system of deposit insurance which is compulsory for the banks, which it is generally admitted do not need it, and only voluntary for the other institutions? Do you really think you are going to accomplish much?

Mr. SLATER: I think, Mr. More, there is a question involved here that I, as an outsider, cannot really answer very properly for you. My own view is the federal government could have said anybody in the deposit business has to have deposit insurance and that is that. The voluntary aspect of this thing is to be regarded as a tactic. The question that is really important here is whether in fact, as Dr. Binhammer put it this morning, when you put together enough of a package of carrots and sticks so that in fact what is voluntary is voluntary but it is a little

like the old volunteers in the army. It has got a lot of suasion about it, a lot of carrots and a lot of sticks and, in fact, becomes something of considerable significance. Now, I do not believe for a minute—

Mr. FULTON: Who is going to be the Sergeant-Major?

Mr. SLATER: Oh, I think there are nominees around. But I do not believe for a minute you should take literally the voluntary character of the proposed deposit insurance. It is going to be voluntary with a lot of sticks behind backs and suasion, and so on. Or else, it is simply not going to do the job that your Committee has to face.

Mr. MORE (*Regina City*): This was the point I wanted to make. You have no more information than we have.

Mr. SLATER: I could not possibly have, sir. I have no privileged position in the government service or with a minister or with the officials.

(*Translation*)

Mr. COMTOIS: Mr. Slater, constitutionally speaking, can a province allow an institution which is a near-bank with a provincial charter, to accept deposit insurance?

The CHAIRMAN: Federal or provincial deposit insurance?

Mr. COMTOIS: Federal?

(*English*)

Can the province oppose a provincial charter of near banks or Caisse Populaire to participate.

Mr. SLATER: Could the province say “no” to the institution if it wanted to get in?

Mr. COMTOIS: Yes.

The CHAIRMAN: I think in fairness to Mr. Slater—I will allow him to answer the question—he might characterize it as a legal question rather than an economic one, a question of economics.

Mr. SLATER: I do not know the answer to this one. I suppose that what I would say is this. If the Caisse Populaire or any other set of institutions are carrying on a set of activities of which one piece is this deposit business in this narrow sense and if, for a lot of the other pieces, there is no question whatsoever about provincial responsibility, and so on, I suppose an institution, whatever its legal right, would be very unlikely to take on this federal deposit insurance and pay the prices that might be exacted of it by the province quite legitimately, completely within provincial power in other matters. The problem, of course, I think, is one must be very careful here. We know that under our constitution governments have complete power. But, on the other hand, I think if a government behaved in an extremely arbitrary manner with respect to its own chartered institutions, presumably there is some recourse in courts and such like, but my guess is that in the crunch, if a provincial government says to institutions which depend in absolutely vital ways on the good grace and favour of the provincial government, that the institution would probably not be willing to take on federal deposit insurance voluntarily if the provincial government said “no”.



It may be a fairly impractical point of view of the thing but it seems to me that is the best I can do for you, sir.

Mr. COMTOIS: Thank you.

The CHAIRMAN: I now recognize Mr. Cameron followed by Mr. Lambert and Mr. Lind and Mr. Gilbert. We are obviously not going to complete this by six o'clock. I presume, Mr. Slater, that you will be available for our meeting this evening?

Mr. SLATER: Yes, I can stay.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Slater, I noticed on page 3, in your paragraph No. 8, you set out the primary criteria for distinguishing banking for the present purpose. It is that whether or not some of the debts of the institution are part of the money supply and whether or not some of the operations of the institution result in changes in the money supply of the nation. Now, could you by those criteria, list the type of institutions, or some of what we have been calling near banks, that would fall within those criteria?

Mr. SLATER: The ones that would fall most clearly within these criteria would be the non-trustee elements of the activities of the trust and loan companies; not all of those but a piece of those activities in which they clearly are engaged in a deposit taking business. You can get cheque books, you can issue cheques, you can make payments, and even some of their claims can be readily used even though you do not formally have a checking privilege. That is one that is fairly easy and straightforward to deal with. It is my impression that some activities of the Caisse Populaire in the major urban centres also fall within this range. There is a set of institutions, we have one in Kingston, Commonwealth Saving and Loan or something like that, which would fall in the category of a loan company rather than a trust and loan company. It is a loan company. It, certainly, and all the institutions that are like it would fall into that category. I believe there are some credit unions that would fall into that category. Those are the ones that are fairly easy and definite, Mr. Cameron.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would that characterize the Alberta treasury branches?

Mr. SLATER: I am sorry, sir, I simply do not know enough about them. It may well be that they are in that position. They have characteristics which—I simply do not know; I will have to simply quit there.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): My next question will be this. Would the operations of these institutions you have listed fall within one or other of the classes of subject within federal jurisdiction as set out in the B.N.A. Act?

Mr. SLATER: I would have thought so, sir, in that classes as enumerated powers of the federal government include currency and coinage, banking, the incorporation of banks, the issue of paper—

The CHAIRMAN: Order, please. I think Mr. Fulton may have a point.

Mr. FULTON: I wonder if Mr. Cameron would clarify it for me anyway. You say classes as enumerated in the B.N.A. Act but which section, section 91 or section 92?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Section 91.

The CHAIRMAN: The federal powers.

Mr. SLATER: The federal powers, the explicit classes include currency, coinage, banking, incorporation of banks, issue of paper money, savings banks, bills of exchange, promissory notes, interest and legal tender. Now, I think that by any reasonable interpretation of currency, banking, issue of paper money—the issue of paper money is a very interesting one, you see. The issue of paper money is in there, as I understand it, because—it is in the same clause as banking—the principal form of money of the country back in the days of the B.N.A. Act was bank notes. In effect, bank deposits have replaced them as the principal element. So, I would think by any reasonable interpretation of those clauses in a modern setting the activities of those institutions would technically fall under those specifically enumerated powers.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then, if in this present revision of the Bank Act, we were to include a definition of banking along the line you have set out here with these criteria, thereby bringing these institutions within the purview of the Bank Act, would you consider they should be chartered? Would you consider they would have to become part of the reserve system of the country, with cash reserves?

Mr. SLATER: Let me deal with the easy one first. So far as I can make out, the cash reserve requirement is not of the essence. It is not the definitive thing because, as I understand it, most of these institutions, if one examines their behaviour over a time, in fact by their own rules of prudence and good management as well as by the regulations of provinces, but primarily by their own rules of prudence and good management, in fact hold cash reserve ratios in relationship to their deposit liabilities on a fairly stable basis and on a basis which is not fundamentally different in principle from the basis that governed our banks before we imposed legal requirements on them.

Now, as to charters, the problem here is, I think, the following. The Bank Act is the charter, in a sense, of a bank. But the Bank Act is charters of banks which combine not only the banking functions but a whole range of other functions. The Bank Act has its characteristic structure, its particular mix, because of the mix of things that banks are. Some of these institutions do a little bit of deposit taking business, some of them do quite a lot and some of them will probably do a lot more no matter what happens. But their mixture of activities is often a very different mixture in other respects from the mixture that the banks carry on. I just do not think it is a very proper or appropriate way to think of simply forcing them to opt into the bank charters, if we think of bank charters as the Bank Act as it now exists because that is the charter. I think that what one would probably have to do is to work out a limited set of requirements that they must meet with respect to the banking elements of their activities and a set of those requirements which made sense in relationship to the Bank Act. But I think I simply would have to quit there and say this raises problems that are beyond me, I think.

The CHAIRMAN: I think it is a good time to quit, not only because of the problems but because it is six o'clock. This meeting is recessed until eight o'clock.

## EVENING SITTING

The VICE-CHAIRMAN: I will now call the committee to order.

At the adjournment Mr. Cameron had the floor and had not finished. I will start with Mr. Cameron, and he will be followed by Mr. Lambert.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I would like to come back to the question of the cash reserves of any institutions which, by definition, have been brought within the present preview of banking. As I recall it, you were in doubt about whether it would be necessary or desirable to call on them for cash reserves and I was recalling the evidence that Mr. Rasminsky gave us when somewhat similar questions were asked of him.

In the first place, in connection with the cash reserves of the chartered banks one of the questions was: why was it necessary to have the cash reserves of the chartered banks set at a level somewhat higher than they would themselves feel necessary for their operations. Mr. Rasminsky reply was that this was essential for his control of monetary policy. Now, it is true that Mr. Rasminsky, with regard to the near-banks, did say that he saw no danger to his control, in the meantime, but he did make a caveat that perhaps in ten years' time, if they continue to develop relatively to the chartered banks, as they have been doing, it might be necessary to consider it.

The question I would like to ask you is this: If we develop a definition of "banking", which brings these institutions within the purview of banking legislation, would it not be better to establish the system of cash reserves for them now rather than to wait until perhaps it became vitally necessary?

Mr. SLATER: I think that the first point that I would make, Mr. Cameron, is that the function of cash reserves in relationship to our banks is not quite as decisive a thing, from their point of view, as it used to be. Cash reserves used to have several functions to perform the minimum operating balances, a kind of precautionary fund, and then quite a large sort of emergency fund, because their own liquidity depended rather vitally on their cash position; because we did not have the sorts of provisions with the central bank and related things, and highly developed markets, that we now have, and which provide many more safety features than we used to provide.

Now, I think I was probably too quickly off the mark and a little cavalier about the matter of cash reserve requirements, with respect to the near-banking institutions.

I think the cash reserves for these institutions again have to be looked at a little as for the banks. They are important to them as an element in their own liquidity operation, in a way, because those institutions often do not have quite the same range of liquidity opportunities; admittedly, they do not have quite the same needs either, but they do not have quite the same opportunities as the banks. They in fact may, in a way, have to have a little bit more of an eye towards their liquidity requirements in setting their own cash reserve requirements than have the banks.

There are two points involved. The first is that it may well be that from the point of view of protection of the public and the current liquidity situation, and the kinds of liquidity facilities that these institutions are carrying on, and the new range of functions and so on, that indeed some of them may be operating with cash reserve practices that are too limited in relation to what they should have. I am sure there is always a certain temptation, when things go well for



quite a time, to start thinking that they are always going to go well, and therefore to sort of trim back a little on your requirements. There may be something in that, and there may be, therefore, quite apart from the control questions, issues that should be looked at on the adequacy of the loose cash reserves positions of these institutions. I simply do not know enough about their actual cash practices in detail to be certain of this.

Regarding the control of the cash reserves as an important link in the operation of monetary or credit policy, there, I suppose, the most important thing is that, whatever reserve practices exist, they be relatively stable—stable either because of the practices of the institutions, or the practices of the institutions with a bit of encouragement, or stable because of some legal requirement.

I think that when Mr. Rasminsky said that he did not think at the present time that he needed cash reserve requirements on these institutions from a control point of view he probably took the view—certainly it is a view that others have taken—that the amount of freedom that these institutions in fact exercise in varying their cash reserve positions from a short term point of view has been somewhat limited; and the Porter Commission evidence tends to support this. I think that it is proper, however, that, on the cash reserve requirements careful consideration be given to the adequacy of their requirements in the light of their needs and liquidity facilities. And undoubtedly additional work and thinking will have to be done on the question of control.

I think that is the best I can do on the cash reserves themselves, Mr. Cameron.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Thank you, Mr. Slater; that is all.

The VICE-CHAIRMAN: Thank you, Mr. Cameron. Mr. Lambert.

Mr. LAMBERT: Mr. Chairman, I am going to take up right from that point. I was wondering why Dr. Slater would think that one would require cash reserves to the same degree as in the past if you have got to bring in deposit insurance, remembering the other aspect of cash reserves, as against being a tool of monetary policy on the part of the Central Bank. Now you are, in effect, doubly insuring a high percentage of deposits in the chartered banks with your proposal on compulsory deposit insurance for the banks.

Mr. SLATER: Mr. Lambert, I would say two things. The first is that the act that is proposed in fact involves a significant reduction in the cash reserve requirements on the chartered banks as compared with what now rules; and, secondly, that the average 12 per cent on current accounts and 4 per cent on savings deposits averages out at under 7 per cent with the present distribution of liabilities.

What is additionally relevant here is that it seems a reasonable expectation, if the act goes through, that the proportion of the bank debts, which are subject to the 4 per cent rate of minimum cash reserve ratios, will increase in relation to the total. Therefore, there is not only the once and for all changeover to a cash reserve ratio, which is now 8 per cent, to something which is below 7 per cent, but there is, in fact, beyond that, a reasonable expectation of some further downward drift.

The second point, I believe, is simply a matter of judgment with respect to the commercial banks. There is no question that the deposit insurance, in a sense,

adds an element of protection to the banks that they did not have before. They may not need it, and it may not make much difference to them, but it is a net addition, and I think you are quite right, sir, in suggesting that that in itself is a further factor in reducing their cash requirements. I think it is a matter of judgment that you would have to explore with the governor of the central bank and with bankers and others on what the right numbers are. Twelve per cent current and four per cent on all things other than current is not a high cash reserve requirement for banks by the standards of this world. Most other places in the world, in fact, have requirements which are, I believe, a little on the higher side.

Did you also want me to say something about the deposit insurance in relation to the near-banks?

Mr. LAMBERT: No, not at the present time; I will come to that. My own view, to comment on what you have said, is that I think 12 per cent is too high. It should be no greater than 8 per cent on the current account, in view of the fact that there is going to be deposit insurance. But that is a matter of opinion and judgment.

I was very glad to read your paper, particularly with regard to your feeling that there should be a definition of "banking" within the act. I have thought of myself as a kind of lone voice on this, with Mr. Cameron and others—a lone voice outside of the Committee, I should say—but you have explored it sufficiently with the others, and I am not going to say any more about that.

However, one point that did bother me in your brief was the comment that the banks, because of the ceiling on the interest rate, had to resort to satellite operations, which you felt would not be necessary now and which were, in fact, not quite proper for the banks. I am just wondering whether you include types of operations like Kinross and RoyNat, because I would like to know whether you feel that the purpose that those two corporations serve at the present time will not be done away with under the new act? Is the medium to long range financing that can be done through those operations going to be satisfied by some provision in the proposed act?

Mr. SLATER: As I would say to my students, "That is a terribly good question."

The VICE-CHAIRMAN: What do they say about the answer?

Mr. SLATER: Sometimes they are not very satisfied.

I think I was just a little fast in sliding over this particular point before. Let me say one or two things in general, and then deal specifically with your question.

I would be quite disturbed if we were to carry through an act which either implied, or encouraged, or perhaps even made necessary, the development by our banks of a lot of specialized satellite institutions, in the way that the Australian banks have done. That is to say, they have developed hire-purchase companies and chopped them up into two or three kinds, and mortgage companies, and so on. This is a very tricky issue, because the principal argument against the extensive use of the satellite procedure, I think, is that the ultimate underpinning of the satellites is the bank's capital and the bank's own position. The bank cannot, in fact, allow one of its satellites to fail. It has to bail it out, if it is mismanaged or something else goes wrong, or if it gets into the kind of game

that turns out not to be viable. Ultimately the bank's capital and the bank's general assets are the things that provide the basic security.

I would be most unhappy, indeed, if we were to get such a satellite development and such a confounding of the relationship between the satellites and the main bank as to make it difficult to understand the fundamental basis of security of the banking system. In other words, I think, under many situations, an extensive satellite development might very well be a weakening in the strength of our banks.

Now, the thing in favour of the satellite development is that you can carve off a special kind of institution to do a special kind of function, and it may be that this can give you an appropriate adaptation of your management, your organization and things of this sort.

Turning to RoyNat and Kinross I think I have to say, in the first place, that I simply do not know enough about these institutions to have anything like a definitive view on them and, therefore, what I say is conditional upon a degree of ignorance.

My impression is that there is a great deal of attraction to the drawing of a bank act with a set of conditions under which we can, in fact, carry on within a bank a broad range of borrowing and lending functions; that there is a great deal of attraction to the so-called department store financing type of approach as compared with the satellite kind of approach. I think that if you draw a bank act that restricts too tightly the scope for your banks to develop a broad range of borrowing and lending functions the banks will very naturally tend to develop satellites. They are going to be encouraged to do that. I think that Kinross is easier to discuss than RoyNat, because Kinross is essentially a mortgage lending operation, and the explicit provisions of the act before you would, in fact, not make Kinross necessary for the Bank of Commerce to be actively engaged in the mortgage business as a bank.

The RoyNat one is more difficult, because the question that you would have to settle is whether you can create a bank act which can permit the banks to have the scope, in terms of their borrowing and lending operations, in terms of interest rates and length of commitments and so on, that permit the banks to do the RoyNat sort of thing within the bank instead of creating this other kind of institution.

It is not entirely clear, because as long as the ceiling stays in place I suspect that RoyNat cannot be run in under the act, because RoyNat ought to be able to lend under current circumstances at rates of 8, 9, or 10 per cent. Those are its lending rates, and it has to be able to borrow at rates of  $5\frac{1}{2}$ , 6, or  $6\frac{1}{2}$  per cent. You cannot do that with the act as now proposed unless if quite a little room opens up in the debenture side and the deposit certificate side. Even then, you are in trouble . . .

Mr. LAMBERT: With respect to house mortgages. I was thinking of this: Why would it not be proper for a consortium of banks and trust companies to get together, each contributing a proportion of the founding capital and the experience if their operations to the establishment of a company which would go into a specialized field? Not only would they then realize upon, shall we say, the value of the knowledge of their own officers but they would combine it with that of people in other banks and trust companies, who may have somewhat analogous skills. As a result, you would get a better operation; you would get a better



meld of experience. I would have thought that this sort of thing in Canada would be encouraged rather than discouraged.

Mr. SLATER: I have had a couple of exchanges over Bob MacIntosh's proposal in this respect, so I have given a little thought to this. It seems to me that on this one—the position that I would take would be: Is the sort of thing you describe possible? The problem, presumably, in drawing the act is to permit a limited number of special function things of this sort to emerge; to impose the proper requirements of accountability and bad debts protection and so on, so that the bank's position, as a bank, is in a sense protected in these things; but not to go so far in permitting the satellite development as to encourage that as the general form of practice of development of our banking institutions. This is the kind of ideal in the world, and I am simply not good enough on the drafting side of this to know whether that is possible.

I think that comes closer to the ideal than anything that I have suggested earlier. I think you are quite right, sir.

Mr. LAMBERT: Mr. Chairman, this is the last area that I want to discuss.

Mr. Slater mentioned something about the possibility of a multi-rate structure in the field of deposit insurance—presumably with the gradation of rates being geared to the type of institution that was in the scheme. However, nothing was said about who would be elected to bear the highest rate.

I am concerned primarily not about the near-bank but about the person who is going to pay for that—the customer. The near-bank customer says: "Well, I have to pay ultimately maybe one-eighth of one per cent". In another institution it might be one-twelfth of one per cent, or some gradation of this kind. Has any thought been given to where the money would ultimately land? Naturally, at the low-rate institution, I think.

Mr. SLATER: I think on this one there is a problem of trying to balance things up. I am not certain about it, but I think it runs a little this way: Quite often the institution which has the riskier business is also the institution which is, in a sense, the one which has inherently higher-income business. In effect, the greater risk and the higher earnings and, on the other side of the picture, the higher rates of payments to depositors, do go together a bit. It seems to me that in looking at this one and asking where will the deposits go the thing one would have to say is: If you had a multi-rate structure, institutions type "A" are borrowing at higher terms, lending at higher terms and they are riskier; that, in a sense, the deposit insurance costs more but it also gives the people more in that situation. In the other situation deposits cost less and give the people less. I am not at all sure that the distribution of funds would be made, as it were, on the basis of differentials in the deposit insurance rates.

Mr. Lambert, all I am saying is that I believe that this thing has to be put together in a sort of total risk, earnings interest rate, deposit insurance kind of package before one can sort out the implications of multi-rate structure.

I should say that my own prejudice in this matter is that there may be on balance, and taking the act as a whole, a pretty good case for a single rate structure, even though you know that you are, in a sense, proposing more than the cost of some and less of others; but one has to look at the bank act as a whole.

Mr. LAMBERT: Surely none of us is under the delusion that we do not know where the cost of the insurance premium is going to eventually land. This is going to be strictly a cost to the customer.

Mr. SLATER: But the customer gets a reduction in his risk, too, you know. The customer gets something for this. The only net cost in this thing is the cost of the inspection operation. The rest of it is not a net cost to the community as a whole. It is a question of—as in most insurance situations—it is a genuine situation where everybody pays a little and out of an insurance situation some people get a lot but the best of all possible worlds is never to collect the premium in this particular situation. I think there is genuine insurance character to the thing, as I understand it.

The VICE-CHAIRMAN: Mr. Lambert, may I ask a supplementary question?

If you really want to have fair competition among financial institutions how can you have it in such a way that the measurement of the rates could be done by other than the lenders themselves?

Mr. SLATER: Mr. Laflamme, I am sorry; I am more “soggy” than I should be. Could you repeat that, please?

The VICE-CHAIRMAN: You were saying that there could be some different degrees of rates regarding insurance. How could it be done by degrees so that the measurement of the risk could be done by others than the lenders?

Mr. SLATER: I think the risk arises to some extent from the kind of assets that the institution owns. If an institution owns a lot of high-yielding pieces of paper, a certain percentage of which is going to go bad, the risk is different than if that institution holds a lot of low-yielding pieces of paper like treasury bills in which the risk of some of the pieces going bad is very low indeed.

I would think, in fact, it is possible, in principle at least, to get some measure of differentials of risk by looking at the quality and the nature of the assets which the institutions own. When British Mortgage owned a lot of pieces of paper, which were Atlantic Acceptance pieces of paper, this was very different from the Royal Trust owning treasury bills.

I do not want to throw rocks at anybody, but this is exactly the point that is at issue.

Mr. LAMBERT: One last question: Do you think that it is practical and feasible to have more than one deposit insurance scheme in this country?

Mr. SLATER: That is: Is it practical and feasible to have schemes which might differ from one province to another?

Mr. LAMBERT: Yes, that is correct; so that there would be a national scheme and one or more provincial schemes?

Mr. SLATER: Well, I do not know the answer to this. My guess is that if the scheme, like one's taxation system, does have at least a minimum degree of common nomenclature, common definitions, common concepts and, in fact, an eye is given to the question of integration of these pieces into something which has a minimum compatibility, one piece with another, I would have thought that it was possible, in fact, to get some way in this.

I am simply drawing an analogy from a tax system. We are, in fact, able to get along with different taxes and different tax policies in various provinces. We

are able to get along without really anything like colossal problems, providing there is this minimum degree of integration of the systems and compatability of the systems. I think I would be inclined, if I were trying to do a job on this, to explore the possibilities along that route.

Mr. LAMBERT: What degree of uniformity do you think would be required?

Mr. SLATER: You would certainly have to have the classifications of deposits that were employed in the various sytems compatible, one place to another—

Mr. LAMBERT: Inspection standards?

Mr. SLATER: The inspection standards presumably will come in on the question of whether you have essentially different degrees of risk and people detect trouble by different standards, and things of this sort.

My guess is that you do not have to have absolutely uniform inspection, but that you have to have a sort of rough compatibility, and to the extent that there is a federal underpinning,—that will probably have a bearing upon the degree of compatibility that you have to have.

I simply do not know enough about this subject to press much beyond that, Mr. Lambert. I think this is a direction worth exploring.

Mr. LAMBERT: Thank you very much.

Mr. LIND: Dr. Slater, I would like to go into the area of interest rates and competition. In No. 21 you say that it is absolutely essential that the interest rate be raised from the present 6 per cent rate. My concern, of course, is that when we take away this ceiling what is going to happen to the small borrower in this country versus the large borrower? Is he going to be treated fairly, or is he going to have to pay a fairly substantial percentage more for his money than will the large borrower?

Mr. SLATER: I think the best answer is that some small borrowers are going to pay more and some are going to pay less. This is very important for us to try and work our way through. To be perfectly straightforward about this, because I happen to be rated as a reputable person—for no good reason—I can borrow from my bank at 6 per cent, and do. But I am very sure that had I gone to my bank 15 years ago, or if I went to my bank now with the kind of position I was in 15 years ago, I probably would have some difficulty in borrowing at the 6 per cent; in fact, I might end up with a personal loan, or I might end up with a finance company; I might end up in a lot of places.

The point is that some small borrowers benefit by the present ceiling and other small borrowers lose. Where small borrowers *in toto* come out is not entirely clear. My guess is that small borrowers *in toto* are probably ending up paying more for their banking resources now than they would if there was not this present tightness of ceiling.

The much more difficult question is: Where does this thing come out when you get the new situation? There, most of us cannot make anything more than educated guesses. Let me put it this way: If we get the removal of interest rates in the banks, or the ceiling gets up quite a way from the present rate on short government bonds, so that there is some range within which interest rates can fall, then I think what is going to happen is that there is going to be some sort of differential in interest rates that the banks charge, and there ought to be some differential in interest rates that the banks charge, because there are two



principal factors that are operative. One is that it costs a great deal more to administer some kinds of loans and manage certain kinds of lending and security holdings by the banks than others; and, secondly, there is an enormous difference in the risks that are involved in various kinds of businesses. We want the banks, in fact, to be able to engage continuously in a business which is not just the most "riskless" and the most "costless" business to run; we want the banks to be put in the position in which they can, in fact, genuinely and continuously serve a broad range of risks and meet costs of administration and so on.

My guess is that if you get any width in the possibilities of interests that the banks can charge you will get quite a wide variety of terms. Some small people will pay more than they now do, but others will pay a lot less than they now do, because they will have open to them opportunities of borrowing from the banks that they do not now have. The banks simply have to ration their credit at this point.

The ultimate question is: What, then, protects the public? The premise of this act is that the public is to be protected by the active promotion, by legislation and by other means, of competition between banks and other institutions, so that no individual is going to be the prisoner of a bank, nor is a bank going to be in a position to take undue advantage of people.

Over and beyond this, however, I think one has to say that there may well be in Canada a set on special considerations for particular groups in particular circumstances, which, for various reasons, ought to be promoted on other than strictly commercial terms. That is part of our way of life.

The position, I think, that is implicit in the act, and in the other elements of the government's legislation in this respect, is that you ought to meet those things head on. There is no reason why you cannot continue to have a whole series of special acts dealing with special situations. There are differences of view about how much of that sort of thing there ought to be, but I do not think anybody is suggesting that all of the legislation that has been developed to deal with special credit needs should be given up.

I do not know whether I am meeting the issues properly for you, sir, but this is the best first crack I can give you.

Mr. LIND: Across Canada it is fair to estimate that there are over 250,000 small independent business people who use the banks for accommodation. If this ceiling is lifted there is no doubt that the great percentage of those who have to use the bank for accommodation are going to have to pass on the increase to the consumer, which will add to our inflationary pressures.

Mr. SLATER: But, sir, admittedly, these people use the banks, but they use a lot of other things, too. They use a lot of other things that cost them a great deal more in terms of borrowing than does their bank accommodation. My next door neighbour is a small businessman, and he uses RoyNat and he has used the Industrial Development Bank. He pays more at RoyNat than he does at the bank. He uses the bank but he uses RoyNat, too. Others use all sorts of schemes of financing. If you are a car dealer you use the bank if you can; otherwise you use the industrial end of the instalment finance companies and the wholesaling of credit, which is going to cost you a lot more than the bank accommodation, too.

The point is that small businessmen certainly benefit by cheap bank interest rates, but they lose by high interest rates and limited accommodation in other things.

If you are going to size this problem up you have got to put these two things together. I am not at all sure—and I really think you have to ask people who are more expert in the credit game than I—that raising the ceiling will, on balance, increase the cost of credit to the small businessman. It is that “on balance” that you have to look at. Look at what interest rates are nowadays. You have a 6 per cent ceiling. The government of Canada, on 13-month paper, paid 5.88 per cent. If the government of Canada has to pay 5.88 per cent to borrow 13-month paper what justification could there possibly be for my borrowing at 6 per cent? None whatsoever. I am being subsidized today by the small businessman who cannot get bank credit because I have a chunk of it. I am not at all sure, in terms of the interest, of equity in our country, that that makes any sense whatsoever.

Mr. GILBERT: What about your idea with regard to classification of interest rates? Would that take care of part of the problem that you have just mentioned?

Mr. SLATER: This is a situation where it is very tempting indeed to say, in effect, “interest rate ceilings do have a function to perform”. We live in a competitive environment, but we do not live in a perfectly competitive environment. The farmer who lives outside a small town in Saskatchewan, which happens to have one branch of one bank, does not have a huge variety of lending institutions open to him. It is true that he has more than we might think, because he can borrow through his co-operative; he can borrow through his elevator company; he can borrow through his implement salesman, and so on; so that there is more there than one might think; but we do not live in a perfectly competitive world. There is the serious question of how much effective protection we are going to have in this country from the competition.

It is awfully tempting to think that you could drop all the bank lending business into three baskets, and say that there is the prime, industrial and commercial customer; that there is a consumer customer, and that there is some kind of small businessman or farmer customer. I do not know you would get these exactly right. It is tempting to say, “Well, there is a rational differentiation of cost of administration and risks, between these broad categories, and as a rough-and-ready rule we would come out with a ceiling of 8 per cent for this group now, and 9 per cent for that, and 10 per cent for that” or something of this sort. You could even put this thing in with a kind of float so that it goes up and down with the short bond rate, and so on. This is very tempting.

I think what you are going to have to do, if you want to explore that, is to ask people who know much more about classifying credit than I do, to see whether there could be any feasible, rough-and-ready breaking of these things into two or three categories that make any sense, and which, although not perfect, would do what ceilings are supposed to do, without doing all these other things that the present ceiling has done, which I think we all regard as a really pretty unsatisfactory set of adjustments.

Mr. LIND: You make a statement here:

The substance of the ceiling has been broken in many respects for many years in Canada.



Getting back to this interest rate again, in what way have these ceilings been broken, in your estimation, and have they always been broken in favour of the banks, or have they sometimes been broken in favour of the borrower?

Mr. SLATER: A ceiling is a limit on the maximum that the bank can charge. Since there is no limit to how cheap the bank can make its services, I think there is no barrier to their being as favourable to the customer as they like.

That particular remark, sir, was written when I was in a little bit of a state of pique, on leave, camped in England, and having received the earlier bill which preserved the 6 per cent ceiling, etc. etc., and I regarded that bill, and I still regard that bill—and the very fact that you have a different bill suggests that I was right in that respect—as just awful.

I think you are all familiar with the sort of things that are involved, and if the 6 per cent ceiling is interpreted as the gross interest rate that the banks can charge for any kind of lending activity, and if the premise is that the banks will recoup most of their service costs by means of the interest, too, then I think it fair to say that quite a lot of bank lending, interpreted very broadly, has been at rates in excess of 6 per cent for quite a long time. I think you can say this without pointing any finger of scorn at the banks, as doing things that are extortionist, or anything of that sort. The most obvious point is that the distinction between the banks buying securities and making loans is a distinction that the lawyers like to make, but it is a distinction that is trivial. The point is that when a bank buys securities to yield more than 6 per cent it is making a loan at more than 6 per cent in any reasonable economic interpretation of making loans.

The second point is the one that has been before this Committee on successive hearings of the Bank Act on several occasions, and it is the way in which the personal loan business is done. There is a variety of things in various banks, and we all know that in gross terms, that is, on a gross interest rate interpretation of the lending rate at which banks carry out their lending—they are lending at more than 6 per cent. We all know that, and that has been going on for more than 20 years in the Canadian banking system. It may very well be, if you examine what the net returns to the bank are, that they are less out of that than they are out of holding government bonds, because you are dealing with a class of business that is inherently costly to do.

Mr. LIND: I am not too much interested in the consumer loan end of it. I am more interested in the commercial aspect, for the small business person. I am more interested in whether, once we remove this ceiling, we can be assured that there is going to be competition between the chartered banks for this small borrower, and in that way keeping the interest rate to him down in an area that he can reach and probably still make a profit in his small operation.

Mr. SLATER: On the competition side I think all we can say is that the general tenor of your act is to attempt to promote competition among the banks, and that the surrounding statements that have been made by the minister are probably to promote additional banking development. The general tenor of the act is to expect that there will continue to be lending institutions carrying out a broad range of lending functions, other than the banks, too, and that out of this will emerge a competitive environment which is satisfactory.



It may well be—and I have no idea what the difficulties are in this—that one would want to have some kind of watching brief on the emergence of the competition and its satisfactory performance and so on. One might very well want to have included in the returns some system that would indicate the terms on which various kinds of lending are done.

I do not know that anybody can assure you at this point that the competition will be adequate. I think that all you can say is that things are being proposed that set you on the road toward that sort of development, and the belief and hope are that these things will come out the right way. I am sorry, I simply cannot go beyond that point. I do not know any more than that about this matter.

Mr. LIND: There is the proposal in Bill No. C-222 with regard to the cutting down of interlocking directorships. Is it your opinion that this will create more competition between the banks?

Mr. SLATER: I guess this is in line with the old problem, that the only fellows who can really tell you the answer are the fellows who have been in the game a little bit.

I often tell my students that anybody who talks about investment ought to have invested a little bit. There are others in this room who will recall that there was another part to the story, that those who are going to talk about girls ought to have gone "girling". Therefore, those who are going to talk about bank directorships ought to have been inside at a directors' meeting and have operated one, which I have not.

Mr. LIND: Which are you competent at?

Mr. SLATER: None of them; demonstrably incompetent at the first; I have four daughters for the second; and I have not been there for the third!

My feeling is that cutting down interlocking directorships and so on is, in fact, a step in the right direction. It certainly cannot do any harm to competition between these institutions. There is an old saying by Adam Smith that I think is a little appropriate for this sort of circumstance, that when businessmen get together it may be for good or ill, but you cannot be absolutely certain that it is for good.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): We could perhaps close all the golf clubs and the clubs.

Mr. SLATER: A man with a Scots accent talking about closing golf clubs! This is awful.

I simply do not know. I have not really been involved in this. My impression is that—

Mr. LIND: You are in favour of—

Mr. SLATER: One of the funny things about the banking business in this country is that banking directorships seem to me to be a little like honorary degrees to some extent, and that bank directors do not, in fact, run banks. There are about two or three men in the bank that run it and it is not the directors, taken en masse. That is the impression of an outsider.

Mr. LIND: Bank directors represent big accounts.

Mr. SLATER: That is like making a donation to a university!

The VICE-CHAIRMAN: Mr. Lind, I would not like to interrupt you, but I must remind you that your 20 minutes have expired. I will allow you to ask one more question.

Mr. LIND: The other question is with regard to this 10 per cent equity position held by the banks in various companies. Are you in agreement with that? Do you think that is a step in the right direction?

Mr. SLATER: I think the proposal, as I recall, is that the banks are to be limited to a maximum of 10 per cent ownership of the voting shares of other companies.

Mr. LIND: That is right.

Mr. SLATER: As a general proposition, I think, yes. I think one would have to qualify it on the point that was raised in answer to Mr. Lambert's question. But, generally, I see nothing but good arising from the banks, in fact, being forced to be on an at arm's length basis with their competitors.

The VICE-CHAIRMAN: Thank you very much. Mr. Gilbert.

Mr. GILBERT: Mr. Chairman, I would like to ask Dr. Slater a very short question on interest.

It arises on page 8 of your brief, in paragraph 22. It says:

Much greater disclosure of charges, and in financial operations will also be required.

This is with regard to banks. Are you suggesting that they do not make this disclosure with regard to bank charges at the moment?

Mr. SLATER: That is rather sloppily written. I think what I had particularly in mind was that if you are going to turn to the competitive route it may well be that one would want a lot more information. By "charges" I mean interest rates and similar charges associated with various sorts of lending operations. I do not think we have anything like really first class information on this sort of thing in the public domain. That was essentially the point.

Mr. GILBERT: But in the present act there is not yet any definition of "bank charges". I thought that was what you were directing your mind to.

Mr. SLATER: "Bank charges" covers a very, very difficult set of issues on which I have just touched the fringe, and I just have not got them sorted out. You have to get away from the current circumstances to get this in perspective. In principle, there is an awful lot to be said for a system by which the banks have one scheme of pricing for one set of functions and another set of pricing for another set of functions, but in fact you chop these things up into pieces and you do not force me to pay a kind of package charge that is not related to the mixture of services that I get. I may be a beneficiary, or I may be a loser out of this. This sort of splitting up of schemes has got a lot of merit, in principle.

It is a very tricky piece of territory to sort out what is in fact the proper way of handling this because you have the essential point of the joint cost element in operations, or a series of places where there is jointness of cost, which is inherently a difficult thing to work out. You have odd-looking cost functions which are also difficult things to work out, and so on. The charges

other than the ones that are explicitly interest charges are the ones that I simply do not know enough about to be at all certain of.

Mr. GILBERT: One other short question, Dr. Slater. If it is the intention to bring the near-banks under the bank act, as are the chartered banks, do you think it is feasible to have possibly a trade-off? At the moment you have banks dealing with short- and medium-term lending, and you have near-banks dealing with long-term lending, corporate services, and trust and executor services. With the change, you have the chartered banks now being able to deal in long-term lending, such as mortgages. Should there be a trade-off, to give the near-banks the right to deal in consumer loans?

Mr. SLATER: And general business loans?

Mr. GILBERT: And general business loans.

Mr. SLATER: Oh, I was only elaborating the question. The question was put in terms of should the near banks have privileges with respect to consumer lending, and I asked whether the question should also include general business loans, because many of them do not have that privilege now.

I think the logic of trying to promote competition certainly is on the side of expanding the lending privileges and the lending opportunities of these institutions. I think that perhaps an important qualification would be this, that to the extent that the near-banks are not exactly chartered banks—and, indeed, it is a moot point whether you would ever want to make them exactly chartered banks, because there is a great deal to be said for what I call the overlapping heirarchy of competition—To that extent, I think one would probably want to go at it something like this: Because the near-banks do some things that overlap with the banks, there are certain things that arise in common, in requirements and so on, and perhaps in scope and opportunity. To the extent that they are different in their borrowing functions, and things of this sort, then presumably one would want perhaps to encourage some continued difference of lending possibilities for them.

I see more difficulty, for example, in some of the near-banks engaging in certain kinds of lending activities than in others. For example, it seems to be pretty hard to conceive of their doing the kind of business lending that is done by the banks, and other kinds of business lending might be possible and easier. In the case of consumer lending, I simply do not know enough about it to sort it out properly.

Mr. GILBERT: It may be that the chartered banks will want to participate in corporate services and trust and executor services. I understand that they do that in the United States.

Mr. SLATER: This is a very important question, and one that I think the Committee must consider very carefully.

At the present time the associations, as I understand them, between banks and trust companies are associations which arise because in many situations the customer needs some mixed package of these services. The bank cannot provide the whole range, and the trust company cannot provide the whole range, and even if there was no ownership arrangement whatsoever between banks and trust companies one must envisage the continuation of circumstances and problems in which some association of these services will be required.



I think there are only two alternatives, if the banks in effect have to divest themselves of positions in trust companies. One is that they develop a trust service, or arrange a trust service, within their own operation. The other is that, in fact, they continue, by means of a series of associations and contracts, to get together with trust companies for particular, essential services.

I just do not know which way to go. I suspect that a bit of both might develop, and I take it that it is a matter of concern to the Committee whether they wish to encourage a line of development in this direction or not.

Mr. GILBERT: I have one short final question. If you again bring them closer together you have the problem of permitting the near-banks to use the credit expansion facilities of the central bank, and also adequate access to the clearing system in the country. These are two other factors which would enter into this.

Mr. SLATER: The first one is easy to handle, and the second one is not so easy, but both, I think, are reasonably straightforward, because, in fact, one can think of there being a kind of monetary base which becomes sorted out among the various intermediary institutions of various classes and, in fact, one aspect of the competition between them is really a competition in carving up that reserve base.

In the present process the trust companies have to get some chunk of that reserve base, either directly or indirectly, and they do. I do not think that the splitting of these associations apart will necessarily alter that as long as the trust companies continue to do some banking business.

With respect to the clearing house services, I think the position there is also fairly simple, that any organization that is going to participate in any significant and active way in the payments mechanism and is creating instruments which are part of the payments mechanism has to have clearing facilities.

As I understand it, and certainly the Porter Commission reported in these terms, those trust and loan companies that are, in fact, active do now have clearing facilities. The Porter Commission reported that they knew of no evidence to indicate discrimination against these people. That is something that you will have to investigate, as I cannot, but it is perfectly clear that if these organizations expand their banking functions in the sense we talked about earlier they must have clearing facilities.

Mr. GILBERT: Thank you very much.

The VICE-CHAIRMAN: Mr. More, on a supplementary.

Mr. MORE: Professor, you speak about their need of adequate clearing facilities. Do you mean to intimate by that that those who are so engaged do not have them now?

Mr. SLATER: I said, sir—and I have no evidence one way or another—that the Porter Commission reported that they had done an investigation on these questions and that they did not find discrimination against these organizations in the provision of clearing facilities.

Mr. MORE: That upsets the evidence that we have had before the Committee in this regard.

Mr. SLATER: That is right. Of course, I think that one has to be perfectly clear about the fact that there is an element of grace and favour involved in this

thing, and that is something you people have to face; but so far as we now have evidence in the public domain, there is no indication of discrimination against these organizations.

Mr. FULTON: Mr. Elderkin would be pretty quickly able to report to us if there was, would he not, because of his interest in both types of companies?

Mr. SLATER: I do not know, sir.

Mr. GILBERT: It would not come under his jurisdiction. It is under the jurisdiction of the Canadian Bankers' Association.

The VICE-CHAIRMAN: I still have four names on my list. I would like to know if you think we will be able to finish by 10 o'clock.

I will call on Mr. Clermont.

Mr. SLATER: I will try to give short answers, sir, for a change.

Mr. CLERMONT: To make my contribution, I will make only one remark, Mr. Chairman, and it is this:

*(Translation)*

Mr. Slater, in the remarks which you have made in your brief, you say that Parliament should define what a bank is. I have read your brief, and my remark, I hope, will not offend you. After having read your brief and listened to your replies to Mr. Fulton's questions, and to questions put by other members, I wonder whether those who are responsible for revising the Bank Act in 1954 were not practical in saying a bank is an institution whose name appears in Annex A of the Bank Act.

*(English)*

Mr. SLATER: I am afraid that I wished it was so. I do not think that Canada, through developments in this respect, is at all unique in the world. The fact is that by any reasonable set of economic tests of the activities of institutions, of the things that we would select as being banking—"banking" in the sense of things which call for special, national, constitutional concern—everywhere we have found that institutions other than the traditional ones—the ones that have been called banks—have taken on these functions to an increasing degree.

This is partly a matter of changes in our technology; partly a matter of changes in the tastes and preferences of our people; it is partly a matter of the different mixtures of financial functions, which are wanted in the community, et cetera. My view is that it is simply hiding one's head in the sand to say that the chartered banks are the only institutions which now require the special treatment that we associate with bank acts. There are institutions in this country that have taken on functions that are very important, indeed, in the payments mechanism. They are, if not always perfect substitutes, so much closer substitutes for the things that we traditionally use as elements in our money supply that their activities matter a great deal in our economic affairs, in exactly the same sense that we have traditionally thought our banks mattered, and I do not really consider it to be very useful to act as if nothing had happened in this respect in the last 20 years.

Mr. MONTEITH: I just have a couple of brief questions. I am sorry, Dr. Slater that I was not here this afternoon to hear what was apparently a very interesting discussion. My questions arise out of Mr. Lind's dealing with the interest rate.

You mentioned your neighbour, Dr. Slater, who borrowed from the bank, RoyNat and I.D.B. I did not quite gather whether you meant that if the interest ceiling were raised he would borrow more from the bank and less from I.D.B., or RoyNat, or what the reference had to do with the actual ceiling on the interest rate.

Mr. SLATER: My idea was the very simple one, that if there is, in fact, in the act, considerable room for banks to take on a wide variety of terms, qualities, et cetera, of lending functions and borrowing functions by the banks which are related to this, then, in fact, I would expect that the banks could, within their own domain, do some of the jobs that are now done by RoyNat, and that, in a sense, RoyNat had to be created to do some of these jobs, as I see it, because, in part, the banks did not have the room for manoeuvre within their own operation to do really adequately what RoyNat was in fact created to do.

Mr. MONTEITH: If the ceiling rate were increased.

Mr. SLATER: My impression, sir, is that the Canadian banks, over the recent period, have become innovators and developers, aggressively attempting to develop better instruments and facilities and so on, and all that one can say is that there are hopeful signs that the banks would, in fact, develop a broader range of borrowing and lending functions if they got some room for manoeuvre to do this.

Mr. MONTEITH: I have another question not quite related to that: I think it is agreed that practically all bank lending at the moment is at the maximum of 6 per cent, and that that has become the minimum. Do you see any danger of a maximum of 7 and a quarter per cent, for argument's sake, becoming a minimum?

Mr. SLATER: I think I would have to answer that the following way. If the present level of general credit conditions were to continue—and we will take, as an index of that, the present rate at which the Federal government has to borrow on treasury bills, plus, let us say, a year and a half paper, and things of that sort—if those rates continue—and their rates are just a shade under 6 per cent at the moment, for the best security of the country—then the question is: How much of a differential would be required for, let us say, a prime borrower—how much beyond that? My impression is that the differentials between, let us say, prime lending rates and this government rate—you will have to check with a banker on this—my impression is that they have traditionally been a little under one per cent, but you know there have been times when it has been over, or a bit under. This would suggest that the prime rate—suppose it is one per cent—would come in at about, let us say, six eight eighths, or six and a half, or six and three quarters, or six and five eighths—somewhere in around there; that it would be scaled up from there, and that, in fact, a fair bit of lending would take place at six and five eighths, six and seven eighths, seven, seven and a quarter, and so on.

I take it that in the judgment of the people who drafted the act the view was that a one and three quarter per cent spread between the ceiling and a short or medium rate, which is a short government rate, was an adequate range within which the banks could do business at a variety of rates.



My guess is that the one and three quarters tends to be a little on the narrow side for the range, but if one bears in mind the fact that the banks are going to be able to open up on the mortgage side of things without a ceiling on their lending rate, and if, on the other side, you see a bank which can borrow on a debenture basis as well as on a deposit certificate basis, and you scale down their cash reserve requirement, it may be that if you put all of these things together the one and three quarter per cent range is reasonably generous; but my instinct tells me that it is probably a little tight.

Mr. MONTEITH: Is it your opinion then—and this has been held out by many advocates of the lifting of the ceiling on interest rates—that there will be any increase whatsoever in interest rates to savings account depositors if this formula in our present bill is followed?

Mr. SLATER: I would guess—and it is only a guess—that two kinds of things are likely to happen. The first is that the banks appear to be in the business of creating a number of new instruments, which are genuine saving instruments, and which are in a sense a little competitive with their own savings departments; but that those new instruments are in fact ones which, by being genuine saving instruments rather than mixed saving and checking account instruments, yield higher interest rates than savings deposit accounts. My guess would be that that kind of development would go on, and that would be one form in which the higher interest earnings of the banks would be passed on to the lenders to the banks.

The other thing is that it is my guess that the banks must probably regard their general savings account rate as probably being on the low side at this point. If current credit conditions were to continue, I would guess that, given the opportunity for better interest and other earnings, they would probably in their own competitive interest, to raise the interest rate on savings deposits.

Part of the problem that the banks have is that their savings accounts are this mixed bag. With their checking accounts and their savings accounts, they have quite a mixture. They had not previously such a variety of instruments by which they borrow. Now that they have got more variety my guess is that they will tend to sort the thing out a bit more, and that the savings account in its traditional role will improve a little in earnings, but that a lot of the improvement will be in the development, and continued development, of these new instruments that the banks are creating, and which are much more directly pure savings instruments.

Mr. MONTEITH: I suppose I should put this question to a practical banker, but how long, in your recollection at least, has the 3 per cent figure on savings deposits been in vogue?

Mr. SLATER: I am sorry; you will have to ask that question of a practical banker. My recollection is—

Mr. ELDERKIN: It goes back to the thirties, I am afraid.

Mr. MONTEITH: The maximum, which has now become the minimum of 6 per cent, has only really been in existence since fairly recently, has it not? It has become a minimum in recent times.

Mr. SLATER: Oh, yes, sir. I think that one can go back and get some sort of measure of it. Even in 1963, the differential between the short government bond rate in the 6 per cent was more than one and three quarter per cent. In 1964, for half the year, the differential was more than one and three quarters per cent, or something of this sort. The point is that you do not have to go very far back in our history to find situations in which there was quite a spread between the government short-term borrowing rate and the 6 per cent ceiling. That gives you some measure of how much room for manœuvre there was.

Mr. ELDERKIN: Mr. Chairman, may I interject on that question that was asked a few minutes ago. It is in exhibit number 10, which was filed on the first day. The present 3 per cent rate goes back only to 1962; before that it was 2 and three quarters; and before that it was two and a half. The 3 per cent rate was in effect in the twenties, but it dropped down after that.

Mr. MONTEITH: The 3 per cent has been in effect since 1962, but the prime lending rate has not been at this minimum of 6 per cent for nearly as long as that?

Mr. SLATER: No; I think that is wrong—

Mr. MONTEITH: The actual minimum has not become the maximum until comparatively recently.

Mr. SLATER: Yes; I think it is appropriate, of course, to remember in this situation, sir, that the share of some reasonably defined savings deposit business that the banks had was also a declining proposition over this period of time that you were talking about.

Mr. MONTEITH: Is it a fair assumption that if the ceiling is raised there will probably not be, other than in certain categories of deposits—in other words, money that the bank is borrowing, which it, in turn, will loan—other than in those various categories which you surmise will come into being, and which have already, to some extent—a noticeable increase in rate of interest for deposits; and that the chief asset, if one might call it that, of increasing the interest rate will be that the bank will not be in a position to loan on different types of loans. In other words, the average depositor is not really going to benefit.

Mr. SLATER: I simply do not know the answer to this, sir. It is very difficult. The fundamental problem is the savings deposit lump, as it now is in the banks' operation, which is such a mixed bag. There are marginal elements of that which are very sensitive to interest rates and earnings and, indeed, the banks have been losing out on this marginal element. There are pieces of the savings accounts which are probably not very interest-sensitive at all. The banks, in a sense, would not get much out of raising the interest rate on them in the sense of holding them, or not holding them, or whatever. I think the real question is going to be the extent to which this sorting out of the present lump of savings accounts into differential pieces takes place. My guess is that if you take the savings customer of the banks, broadly defined, and give him his new opportunity to spread his savings, some in a savings account, some in this and some in something else; he is, in fact, going to be able, if he wants to do so, to get a significant improvement in his earnings.

I think it is going to be very much in the banks' own interest—and certainly the things that have happened in the last year and a half tend to confirm this—to compete aggressively for these important marginal elements in the savings load.

It is true that a little old widow, who holds her funds in a savings deposit account, no matter what, is probably not going to get very much larger interest on her account. What we hope is that in fact she is going to get better advice than she had in the past on how to manage her account, too. That, of course, is the crucial element in the outcome here.

Mr. MONTEITH: One final question, Mr. Slater: Can you foresee in the future any time when the present formula, as proposed in the bill, will free the interest rate entirely so there will not be any ceiling?

Mr. SLATER: This is by no means impossible within the life of this act, because the important thing for us to remember about this is that the ceiling is floating in relationship to the short end of the government bond market. It is an inherent feature of interest rate structures that the short end varies more widely than does, say, the medium-term government bond. You get an easing of a certain degree, a certain number of points, in the middle, and you get, proportionately, more points in the short end. Therefore, in terms of the over-all credit conditions in the country you do not have to have a huge easing to make quite a difference at the short end of the market.

I think it is fair to say that it is more likely that we are in for several years more of relative credit tightness than relative credit ease. It is more likely, therefore, that the ceiling would remain on than come off. There are, I think, two main reasons, for this. One is that we do have ahead of us in Canada, North America, generally, and in the world—even though population growth is beginning to slow down a little bit—a stretch of years in which the population growth in the critical age ranges is going to be fairly large and in which the capital requirements that come from that are going to be large. There is no indication we are high savers; there is no indication that we are going to be greater savers; so that is one of the fundamental elements that tend to keep credit tightness in place.

The other is that there is a view that we have some uncertainties in the world monetary system which tend to impart a bit of a bias in the direction of credit tightness in various national positions, as a by-product of the general international setting.

These two things together are, I think, probably the main factors that are likely to give us a general medium term outlook of credit tightness. But we are almost bound to get some ebbs and flows within that and I simply cannot tell you how big these ebbs and flows will be.

The point I would make is that you do not have to have really huge changes in credit conditions to make a fairly substantial change at the short end, and therefore to free this rate. If I had to lay bets today I suppose they would be that for the next five years, 80 per cent that the ceiling will be on, and five years from now 20 per cent against, or perhaps if I was really optimistic, 70-30 per cent. It is that kind of situation.

Mr. MONTEITH: Thank you very much.

An hon. MEMBER: You are not really very optimistic.

Mr. CLERMONT: Mr. Chairman, may I ask a supplementary to a reply made by Mr. Slater to a question posed by Mr. Monteith regarding RoyNat.



No doubt I misunderstood you, Mr. Slater, but did you say that if, when RoyNat was established in 1962, there had been no ceiling it would not have been necessary to create such an institution as RoyNat?

Mr. SLATER: I certainly did not intend to say that. What I did intend to say was that the kinds of functions that RoyNat performs could probably have been done, in part at least, by the banks if the bankers had had more room to manoeuvre.

In fact, if you go back on our post-war record there have been a number of periods of time in which the banks opted actively and aggressively into the term lending operation, and they opted in and were shopped off about three times. Everytime they got going at it they came upon a patch of credit tightness which knocked them back. Therefore, we do have, in the experience of the Canadian banking system itself, some evidence that they have opted into that kind of activity in the past.

The VICE-CHAIRMAN: I have still Mr. Leboe and Mr. Fulton on my list. Mr. Leboe, please?

Mr. LEBOE: I hope I shall not be very long. I just want to say that it is nice to meet Mr. Slater again. We met about ten years ago, I believe, on a television program down in his city.

The VICE-CHAIRMAN: Was it a good performance at that time?

Mr. LEBOE: I have been listening all afternoon to the evidence that Mr. Slater has been giving us. There is one area that has not been touched on and perhaps you might like to comment on it. It is the situation that arises through the operation of the Bank of Canada when we talk about competition among banks. It does seem to me that, necessity being the mother of invention, the banking system has been reaching out to try to get more than it has been getting because of the effect of the 6 per cent ceiling.

On the other hand, where you have a tight money policy that is going to continue as you say, for perhaps another couple of years, it seems to me that it is very difficult to get competition amongst the banks when they are at the limit of their lending ability.

Does this to you as a student of banking, pose a problem in your thinking?

Mr. SLATER: I think when they are at days the limit of their ceiling of course they cannot compete in interest terms on loans, but my impression is that the banks have, willynilly, engaged in a lot of competition in a lot of ways in these years, even with the ceiling, in part because, I take it, that the judgment is that, one way or another, they simply have to get out and scramble.

They certainly compete for large deposits and they certainly compete in deposit certificates. They certainly compete in trying to promote their consumer lending business. I gather from some quarters that they compete too much in certain respects, with bank openings and smiling girls and things of this sort; but the point is that they must regard their position as one in which they have been in business for a long time, and with the ceiling they have had to turn their competition in other directions, in effect.

Mr. LEBOE: I was thinking more of it more from the viewpoint of interest rate.

Mr. SLATER: They simply are not able to compete in the interest on loans, as such.

Mr. LEBOE: In other words, this is a part of the tight money policy, and there is no use playing with the banks in this situation.

Perhaps we are looking in the wrong direction to solve our problem when we deal with it from the banking point of view. We should, perhaps be considering immigration, or other things, which may be far more effective in bringing an end to the tight money policy?

Mr. SLATER: It might well be.

Mr. LEBOE: I think it is related to that.

Mr. SLATER: The thing is that it is not completely immaterial to the tightness of ease of credit conditions what kind of competitive arrangements you have between various financial institutions; but on the other hand the central points about tightness of credit conditions are not to be explained by things that are part of the current banking rules, or things of this sort. What the current banking structure rules do is give to credit tightness particular forms or shapes, but the fundamental points about the tightness, I think, lie elsewhere.

Mr. LEBOE: That was the point. We, as members—I am sure I can speak for the rest of the members—hear a lot of criticism aimed at the banks and the Bank of Canada because of the situation, and I think we should be looking elsewhere to try to solve the problem.

Mr. SLATER: I think the Bank of Canada is quite prepared to shoulder its responsibility: The governor has said, for example, in his Per Jacobsson lecture, that credit conditions are our responsibility, within limits of course, which are set by some other things; but we are quite prepared to take responsibility which is ours.

The CHAIRMAN: Are you through, Mr. Slater?

Mr. SLATER: Yes, thank you.

Mr. FULTON: I think I can confine myself to two questions, Dr. Slater.

I want to return to the question of the deposit insurance scheme. You said that deposit insurance would not be effective unless there was, in effect, a stick-and-carrot combination to bring the non-bank financial institutions under such a scheme. Is that a fair summary?

Mr. SLATER: Yes; I think that is a fair summary.

Mr. FULTON: I am wondering whether you have any more specific suggestion on what those carrots and/or sticks should be?

Mr. SLATER: Point one, I think that it is in fact a carrot that the deposit insurance facility for, let us say, near banks—if this is the way it evolves—is in fact subsidized by the existing banks. They are getting something more than they are paying for in this respect.

It is a carrot, I think, if the institutions which opt into the inspection, and so on, which goes with the deposit insurance, can count on lender-of-last-resort facilities, directly or indirectly, because that matters to them.

It is a stick if the provincial governments come into their institutions and say, "You may volunteer; we are going to encourage you very strongly to

volunteer; in fact, we are going to have a general policy of volunteering you for this operation." There are these sorts of things.

Professor Binhammer raised before the Committee another whole range of territory that must be explored, to the effect that it may well be, and it was Dr. Binhammer's suggestion, that for some classes of these institutions cheap mortgage money in some circumstances may also be something of a carrot.

I am not sure about you would put these together. The first three, I think, are fairly clear. That is, the subsidy element, the lender-of-last-resort facilities, in a sense—a clear improvement in what those may be—and the influence of provincial governments, which surely must be concerned with cleaning up and helping to improve the performance of their institutions.

That is about all for this particular round.

Mr. FULTON: I must say I do not quite see the relation of the lender-of-last-resort to the deposit insurance scheme.

Mr. SLATER: The point is, presumably, that if you are in fact in, and you get into situations where you need an emergency supply of cash, if you have been a reasonably good boy, it matters an awful lot to you that you can count, almost, as a matter of right on emergency supplies of cash on fairly favourable terms. It is material to the experience of British Mortgage and Trust and the related trust-company ripples which came out of that.

Mr. FULTON: Mr. Slater, if had had their deposits insured and presumably, thereby, had been under a control inspection system and had had to maintain certain reserves they would not have got into that trouble, would they?

Mr. SLATER: I think the record on this, Mr. Fulton, is that there is no substitute, in the ultimate clutch, for having access, directly or indirectly, to the central bank. There are a lot of things that can happen to you as an institution, even if your institution is well-managed and so on. There are in the United States quite good banks which are subject to deposit insurance and which find themselves from time to time exposed to "runs" even today. If one or two savings banks get into a shaky position and people start questioning other institutions things can happen pretty quickly. They still do, and we still have possibilities of this. It is the fire that you hope does not break out, and the chance of it is not great, but if it ever happens it can do terrible damage to you, and you have to mount the fire-protection operation very quickly. It is not at the absolute fundamentals of our position now, but it is still something that we cannot entirely rule out. It is something of some significance.

Mr. FULTON: I will not press the point of the relationship of lender-of-last resort to deposit insurance any further. I will try to do some studying on it myself. However, it appears to me that you are saying that both of them are potentially legitimate instruments in the control of monetary and credit policy and in the insurance of sound financial institutions.

Mr. SLATER: To supplement and complement one another, I think.

Mr. FULTON: Yes. My final question then is this: Assuming that the deposit insurance system is effective, by a combination of carrots and sticks on whatever other devices are used, to bring in these other institutions, do you feel that the



chartered banks even then should be included automatically, that is, by compulsion? Do you think that their inclusion in a system of deposit insurance is a necessary element to make it effective?

Mr. SLATER: On balance, I would say yes, because it is not going to cost them much; it is going to be based upon the deposit insurance being something which is a part of the general banking development; it is going to cost them something; it is going to impose something on them; there is no question about that; but in looking at their over-all position I think the question really is: What is the whole package that they are getting? There are some things that are going to cost them something and other things from which they are going to gain. Are they, on balance, being treated in a reasonable and equitable manner? I think that is the question.

Mr. FULTON: Is this another unfair competitive disadvantage? They do not need deposit insurance to make them sound. Is this a price it is fair to exact from them to ensure that other institutions are sound?

Mr. SLATER: It is not "other institutions" in an indiscriminate way. It is "other institutions" to the extent, and in the way, that they are, in fact, getting into a banking type business. You are putting the other institutions into a general banking net, and there is some attraction in doing that because you are presumably going to bring banking standards to the whole thing. In terms of structure in your charges you are going to bring some of your traditional banking standards into it, and that seems to me to be an attraction. It seems to me that in these situations one is always faced with doing things, and that you produce a rough, over-all kind of justice, and a rough, over-all justice almost inevitably has about it some discrimination against a particular group in some situations, and for a particular group in other situations. I personally would not worry too much about the banks being discriminated against in this particular respect. Of course, they are going to be discriminated against, but the question really is in terms of over-all rough justice are the banks being dealt with equitably? I think, presumably, that you may be discriminating against them in one respect and discriminating in their favour in some other respect, and there is balance in the over-all package.

Mr. FULTON: I could be mean, perhaps, and ask you in what respect you are going to discriminate in their favour? What is the *quid* that they are getting for the *quo*? Is that a fair question?

Mr. SLATER: I think it is fair to say that the banks get their fundamental lender-of-last-resort facilities out of the central bank for nothing. They do not pay for those.

Mr. FULTON: They say not, because they are not given interest on their reserves. They say they are paying for that.

Mr. SLATER: To make an argument for the banks being paid interest on their deposits, you can probably produce a more equitable package out of this sort of scheme. It is a tricky kind of argument and I would be prepared to lay it out for you as best I could on paper. You could make a pretty fair argument for the banks and anybody else being paid interest on their reserve deposits.

I think you could make a very good argument that the banks are given a pretty fair over-all opportunity for their profitable operations in this country.

They are given a set of privileges in their position; and they have, I think, for a long time probably regarded themselves as privileged in a certain sense, and as carrying enormous responsibilities.

I think it is fair to say that, whatever criticisms we make of our banking system, we should do this from the starting point—and I hope this will not be regarded as silly or naive—that you have a system which, by the standards of this world, has been a pretty good performer.

Mr. FULTON: I agree. I have one final question. Would it be a fair summary of your last reply to say that if the banks are going to be compelled to join a deposit insurance scheme it reinforces their argument for interest on their reserves, or on some portion of their reserves?

Mr. SLATER: That argument, I think, has to stand on its own merits. The fundamental argument about is not because of deposit insurance but is in terms of some other criteria which I am not sure I could even untangle right now. Let me put it this way. In so far as one is building up a package of over-all benefits and responsibilities and privileges and terms and conditions for the banks, to the extent that they subsidize a deposit insurance system then in any reasonable sense of equity one would want to take that into account in striking one's balance, I would think.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): May I ask a supplementary on that? Did I understand you, Dr. Slater, to say that the lender of last resort must, in the final analysis, be the central bank?

Mr. SLATER: Yes, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would that imply that the near-banks, to whom you are proposing we should accord this privilege, must become part of our general reserve system in Canada?

Mr. SLATER: It does not necessarily follow, sir, because it is possible to attach any particular set of financial institutions on to the lender-of-last-resort system either directly or indirectly. In the case of the trust companies, and in the aftermath of the British Mortgage and Trust problem, there was clearly an enormous effect of lender of last resort function mounted even though the trust companies did not in fact have positions vis-à-vis the Bank of Canada directly. It was done, as I understand it, by the Bank of Canada in a sense making its lender-of-last-resort facilities available to the banks, which, in turn, operated vis-à-vis the trust companies, and, I gather, one provincial government which became involved, too. This whole thing was done, so that it does not necessarily follow, sir.

The VICE-CHAIRMAN: Mr. Slater, I now have the agreeable duty of thanking you, on behalf of every member of the committee for your important contribution to the evidence before us.

Next Thursday we will start with Mr. Neufeld of Toronto University, and in the afternoon we will have Mr. Ziegel from McGill University.

The Committee is adjourned until Thursday at 11.00 a.m.

## APPENDIX W

## DEPOSIT INSURANCE—ITS HISTORY AND PURPOSE

H. H. Binhammer

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*Origins*

The protection of depositors' accounts in banks has a long history. Early banking legislation in both the United States and Canada attempted to protect holders of bank deposits as well as bank notes by making stockholders of banks subject to what was referred to as double liability. This method was later replaced by the establishment of "safety fund systems". Legislation introduced by the State of New York in 1829 required all chartered banks of the state to pay an amount equal to 3 per cent of their capital stock to provide a fund out of which the notes and deposits of insolvent banks could be paid. The system unfortunately was doomed after the rush of bank failures following the monetary panic of 1837. This early New York legislation, and later the redemption fund of the National Bank Act of the federal government, were closely followed in Canada in 1890 when a Bank Circulation Redemption Fund was established. This Fund, however, was to protect holders of banks notes rather than deposits.

After the turn of the century many of the American states introduced legislation instituting insurance or guarantee systems, most of which eventually failed. The reasons cited for their failure include inadequate regulation of banks with respect to both statutory requirements and the quality of supervision and the temptation provided by insurance toward ill-considered expansion and reckless loan management policies. The more fundamental underlying factors in the systems, however, was probably the economic recession following World War I and the depressed conditions in the agricultural stage throughout the 1920's.

At the federal level, starting in 1886, 150 bills were introduced in Congress before the establishment of the Federal Deposit Insurance Corporation and the Federal Savings and Loan Insurance Corporation in 1933-34. Deposit insurance administered at the federal level was long opposed because of the disputed jurisdiction over matters involving banking and because of the dismal failures of the state schemes.

Apart from the two federal schemes in operation in the United States today, Massachusetts and Connecticut still have plans insuring the deposits of mutual savings banks. In Canada, aside from some mutual insurance schemes for the locals of credit unions, there are no provisions which directly guarantee or insure deposits or other accounts in financial institutions. The Porter Commission did "not see the need for imposing a general system of deposit insurance". Mr. Sharp, however, when introducing the decennial revisions to the Bank Act, on July 5, 1966, announced that "The government intends to introduce legislation during this session to establish a crown corporation in which the banks and other federally incorporated institutions would be required to have their deposits insured."

*The Federal Deposit Insurance Corporation*

The Federal Deposit Insurance Corporation (FDIC) in the United States was a natural development of the unprecedented banking crisis of 1932 and 1933



and of the character of the American banking system. It was a way of introducing sound banking procedures on a dual system (state and federal) without the fears of federal interference of states' rights. It was a way to ultimately control "overbanking" and ruinous competition among unit banks. Paradoxically, Canada intends to introduce deposit insurance not to control competition, but to stimulate it.

The FDIC was initially established with capital provided by the Treasury and the twelve Federal Reserve Banks. Legislation enacted in 1947 directed the corporation to retire its capital stock as rapidly as possible. The corporation is managed by a board of three directors; the Comptroller of the Currency and two others who are appointed by the President of the United States with the advice and consent of the Senate for six-year terms.

The FDIC was originally established to serve three major purposes. It was to restore confidence in the American banking system, to provide protection to depositors who were not in a position to judge the quality of a bank, and to provide for the improved supervision and examination of banks that were not members of the Federal Reserve System.

Confidence in the American banking system had been shattered during the 1920's and early thirties when thousands of banks were forced to suspend their operations. As banks failed, particularly larger ones, the public ran to them for cash and monetary panic ensued. Deposit insurance was one way to give the public some confidence in the banks' ability to pay and thus stop runs. As a result of the threat of periodic runs sound banks had to keep larger reserves than were normally considered necessary. Insofar as deposit insurance would provide confidence in the banks and stop runs, the economy would benefit from the elimination of the deflationary nature of the higher reserves held by the sound banks.

Another way to assure confidence in the banking system was to improve the quality of bank supervision. Federal deposit insurance was a way out of the morass of disputed banking jurisdiction. All national (federally chartered) banks as well as state banks that are members of the Federal Reserve System are required to insure their deposits with FDIC. State Banks not members of the Federal Reserve System may have their deposits insured if they are able to satisfy the requirements of admission established by law and applied by FDIC. The classification of insurable state banks include commercial banks, mutual savings banks, trust companies, industrial banks and other banks "engaged in the business of receiving deposits."

In determining an institution's qualifications for membership the FDIC considers its financial history, the scope of its corporate powers, the adequacy of its capital, the character of its management, its services to the community and its prospects for future earning power and solvency.

Despite co-operation among supervisory agencies there has been some confusion over the supervision of banks in the United States. For instance, the Comptroller of the Currency supervises national banks, Federal Reserve examiners examine all banks belonging to its system and the FDIC examines all insured banks which include national and state banks and non-member and member banks of the Federal Reserve System. In addition, the states themselves have banking authorities to supervise the banks they charter. It has been suggested, on more than one occasion that a single examining authority at the

Federal level be appointed. It is hoped that when applying more supervision the Canadian authorities attempt to prevent the proliferation of examining bodies found in the United States.

While most of the American institutions conducting a banking function have become members of the FDIC, some have refused to join because they have interpreted the qualifications, as well as the supervision that follows, as unwarranted interference of the federal government in "private business". Others feel that because of the smallness of the risk of failure, the cost of insurance is too high. By and large, however, for most institutions these objections have been not as important as the competitive advantage gained by belonging to the FDIC as the public has grown more and more aware of the protection provided to them by deposit insurance. This same kind of advantage, while not significant for Canadian banks, would be important for our "near banks".

The FDIC protects deposits in three ways. It may act as a receiver of a failed bank and pay each depositor's claim. Originally, the maximum deposit claim allowed was \$2,500, which was later increased to \$5,000 and in 1950 to \$10,000. It has been suggested that the maximum should be increased still further as a result of the increase in the average size of deposits. Payment of claims may be in the form of a cheque drawn on the Corporation's account or in the form of a transferred account in another insured bank which may be a new or an established bank. The FDIC may also make a loan to, purchase assets from, or make deposits in the insured bank on the verge of closing because of financial difficulties. In the United States only one unit bank often serves a community and therefore the FDIC may make every attempt to keep a bank solvent in order to assure adequate banking and financial facilities in the community.

The Corporation may also provide aid by facilitating the merger or consolidation of a bank in financial difficulties with another bank. The Corporation guarantees the bank that "takes over" against loss. The practice followed in recent years has been for the Corporation to facilitate mergers of insured banks in financial difficulty with sound banks. In effect, therefore, depositors are protected not only to the maximum amount of \$10,000 but also for the full amount of their deposit.

The chief source of the assets of FDIC is the payment of assessments or "premiums" by the insured banks. These are fixed at an annual rate of one-twelfth of one per cent of average total deposits. Since 1950 banks have received a rebate as the FDIC allocates 66 2/3 per cent of its revenue after allowing for its surplus account and expenses, back to the banks as a credit. As a result, the cost of insurance now actually amounts to approximately half the quoted rate of one-twelfth of one per cent.

The basis of assessment has been criticized by those who feel it should be based on the average total of the insured portion of accounts rather than on the average of total deposits on the books of the insured banks. It is argued that the present basis has the effect of placing a disproportionate burden upon the larger banks whose average deposit accounts are far above the \$10,000 insurable amount. As a result, assessments are not levied according to the incidence of risks. For instance, a bank that holds a million-dollar account of a business corporation pays its assessment on the full account while only \$10,000 of it is insured. It has been suggested that assessment should be based on risks which



might be calculated on the basis of types of loans, maturity of loans and the capital and reserves of insured banks. If the intended Canadian legislation is to encompass both the banks and the near banks, an assessment policy based on risks would seem preferable to one based on deposits.

### *Deposit Insurance and Banking Competition*

Mr. Sharp has stated that the introduction of deposit insurance in Canada "would contribute substantially to our (government) objective of greater competition and flexibility in our financial system". One can argue that in the absence of deposit insurance, a market structure with a large number of institutions doing a banking function, can not be maintained because depositors seek out the protection of prestigious institutions. A new unknown entrant would have a difficult time. Thus, deposit insurance is required to maintain a large number of banking institutions and a competitive structure.

Will a competitive banking structure best serve the public in terms both of the cost and availability of banking services? To answer this question is to answer yet another. Will a competitive system provide the kind of efficiencies desired and at the same time be failure-proof? Excessive competition or "overbanking" in the United States from 1900 to 1920 resulted in excessive failures in the following decade. To preserve a competitive structure and at the same time make the system failure-proof, the FDIC was established. Its success, to date, in making the system failure-proof is, in large part, the result of its supervisory and examining procedures. One of the early arguments against deposit insurance was that it would encourage "bad" banking since poorly managed and weak banks are placed on the same competitive level as well managed and sound banks. This has not been the case because of the supervisory and examining role performed by the FDIC which has, by and large, imposed sound banking principles on its members who at the end of 1960 represented 97 per cent of all commercial banks which held 99 per cent of all commercial bank deposits. One can, however, argue that FDIC has really not been tested. If a testing time similar to 1932-33 were to arise, would it be able to maintain its excellent record of deposit protection? While this question may be purely academic, the Corporation has a \$3 billion drawing account with the Treasury and Congress would, no doubt, make additional funds available if required.

### *The Federal Savings and Loan Insurance Corporation*

In the United States the Federal Home Loan Bank Board supervises the operations of the Federal Home Loan Bank System which is a pseudo-central-banking system for thrift and home-financing institutions. The twelve Home Loan Banks in the system provide a credit reservoir for member institutions by making advances to them as needed to meet unusual or heavy withdrawal demands and demands for home mortgage credit. Membership is voluntary for insurance companies, of which none are members, and non-federally chartered savings and loan associations and savings banks.

The Federal Home Loan Bank Board Under the National Housing Act is also responsible for the Federal Savings and Loan Insurance Corporation (FSLIC). The operations of this Corporation are very similar to those of FDIC. Savers and investors in member savings and loan associations are insured against financial loss up to the statutory limit of \$10,000. However, as with the FDIC, in practice, one hundred per cent protection is given because of the Corporation's actions to



prevent liquidation of member institutions in financial difficulty. Such actions under statutory authority may take the form of cash contributions, an outright purchase of all or part of the institution's assets, or the granting of a loan. Up to March 31, 1966, after thirty-two years of operation, the Corporation had handled 57 insurance cases involving a loss. In thirty-three of these cases cash contributions were made, in fifteen assets were acquired, and in one a loan was extended, while eight passed into receiverships. In most of the forty-nine default prevention actions, the institution involved was either rehabilitated or merged with a stronger association, with the result that all savings accountholders were protected in full, regardless of the size of their accounts.

While the FSLIC can borrow from the U.S. Treasury up to \$750 million for insurance purposes, its operation has been self sustaining through regular insurance premiums which are the same as those assessed by the FDIC. However, as a precautionary measure, since 1962 members of the FSLIC have been required to pay additional premiums which are, in effect, prepayments of future regular premiums. These additional premiums are based on a rate of 2 per cent of the annual net increase in savings capital of each member, less any requirement for the purchase of stock of the Federal Home Loan Bank. The Corporation credits prepayments to a secondary reserve which earns interest at a rate equal to the average return on U.S. Treasury obligations held by the Corporation during the year.

Savers receive protection not only through insurance, but also through the qualifications required by associations to remain members of the FSLIC. For instance, member associations must maintain substantial loss reserves. In 1964 these amounted to 7.67 per cent of their savings.

### *Conclusions*

There appears to be little evidence to support a conclusion that deposit insurance would make our chartered banks more competitive, more efficient or more failure-proof. The same may not be true for the near banks. The introduction of deposit insurance for them alone, would certainly increase competition among them with the chartered banks. Since there seems to be no good reason why the chartered banks should have to contribute to a deposit insurance fund not really required by them, the government might achieve its goal of providing more competition in an alternative way. It might consider establishing a crown corporation, along the lines of the American Federal Savings and Loan Insurance Corporation (FSLIC), which although a completely separate agency, operates in almost every respect similar to that of the FDIC. Such a corporation would not only provide deposit insurance for the near banks, but would also, through membership qualifications and supervisory and examining functions, establish national standards for the sound operation of near banks. Federally chartered near banks would be required to join while others could do so on a voluntary basis. Judging from American experience, where by December 1964 more than 96 per cent of all savings in the entire savings and loan business was held by associations insured by the FSLIC, near banks in Canada would fairly quickly become members of a Canadian Deposit Insurance Corporation.

In the United States both the FDIC and the FSLIC are primarily interested in the solvency of individual financial institutions and not in the broader question of economic stability. Since there has been some concern over the effectiveness of monetary policy as a result of the growth of the near banks one might

question why the Minister of Finance would not try to kill two birds with one stone, and instead of introducing a deposit insurance scheme allow the near banks access to the Bank of Canada's discount window. Deposit insurance does not assure complete liquidity in the face of a run on financial institutions, or does it attempt to control overall liquidity, as does access to central bank discount privileges. The reason, therefore, for the government's intention to introduce deposit insurance rather than allowing the near banks the discounting privilege must be that of banking jurisdiction. Allowing the near banks discounting privileges probably implies a much closer relationship to the federal government and its control than is the case with a deposit insurance corporation. The Americans certainly used the letter to overcome some of the hurdles of disputed banking jurisdiction. The results have been most successful.

## APPENDIX X

## THE 1966 REVISION OF THE CANADIAN BANKING ACTS

A Comment on Some Aspects of Bills C-222 and C-190,

First Reading,

June-July, 1966.

(by David W. Slater, Queen's University, 31 October, 1966)

1. These comments are intended as a small contribution toward the deliberations of the House of Commons Committee on Finance, Trade and Economic Affairs concerning Canada's 1966 Banking Acts. Attention of the Committee is directed to other comments by this writer on these subjects, including:

"Decennial Revision of Canada's Banking Acts, A Preliminary Report on the Proposed Legislation", *The Canadian Banker*, Autumn, 1966 (copy attached);

"Reforming Canada's Financial Structure", *The Banker* (England), May, 1966; and

"The 1965 Revision of the Canadian Banking Acts" mimeographed and submitted to the House of Commons Committee on Finance, Trade and Economic Affairs when the 1965 versions of Canada's banking legislation were first considered.

2. This brief deals mainly with one set of issues, *the definition of banks and the constitutional and institutional aspects of controlling banks and "near-banks" in Canada*. Brief comments are offered on other issues, including the interest rate ceilings for banks, and on measures to improve the competitive structure in Canadian banking affairs, but these are mainly to revise the writer's earlier comments in the light of new developments.

3. The responsibility for this brief is entirely personal. The writer performs a limited editorial function for *The Canadian Banker*, the journal of The Canadian Bankers' Association, but the views in this brief do not necessarily correspond with the official position of the Association.

4. In this writer's judgment it is within the powers of the Parliament of Canada to define banking activities and to prescribe laws and regulations to govern the operation of such institutions, and it is recommended that such definition be attempted. Also, it is held that the approach to laws and regulation of Canada's diverse banking institutions would be improved by an explicit definition of banks. A flexible programme of adapting legislation, institutional connections and regulations within Canada's financial structure could still be managed, but a better design would be facilitated by the definition. The function of the courts is to adjudicate but not to initiate changes in banking laws. The required scope for banking laws changes in response to new economic conditions and new institutional and public practices.

(i) *Prime Banking Functions of Multi-Functional Institutions.*

5. Canada's chartered banks are multi-functional. They engage in short and medium-term borrowing and lending; they are the principal vehicles in the



internal payments system for Canada; they are the leading dealers in foreign exchange; they act as agencies for collections, and for the purchase and sale of Canada Savings Bonds; they perform safe-keeping functions; and so on. Because the chartered banks are multi-functional, their functions and characteristics, in total, are difficult to define; the Bank Act covers many subjects because the legislation deals with many facets of a particular group of many-functional institutions.

6. Most of the financial institutions which compete with Canada's chartered banks are also multi-functional; and many of these functions overlap with those performed by the chartered banks. Some of these competitors of the chartered banks are incorporated under federal and some under provincial laws.

7. However, out of all the characteristics and functions of banking institutions, one set are primary. Institutions are not regarded as banks and therefore are not subjected to certain kinds of special regulations unless they perform these functions. Institutions which perform these functions, regardless of what else they do or how they were created, are banks. These criteria are necessary and sufficient to define banks and to set the relevant domain for special banking legislation, regulation and facilities.

8. The primary criteria to distinguish banking for the present purposes is whether or not some of the debts of the institution are part of the money supply of the country; and whether or not some of the operations of the institutions result in changes in the money supply of the nation.

9. Nearly everywhere the sovereign has the power to create or to regulate the creation of those things which are the money and currency of the nation. This is, in part, to protect the holders of the constituent elements of the money of the country against arbitrary, unpredictable, perhaps negligent or fraudulent, changes in the qualities of their monetary holdings. It is in part also because changes in the quantity of money in a country have long been regarded as major determinants of inflation and deflation, prosperity and depression, economic growth or stagnation, and strong or weak competitive positions in international trade and payments.

10. Since most of the money in Canada consists of debts of chartered banks and since banks working on fractional cash reserves can influence the quality and quantity of the nation's money, the exercise of monetary responsibilities by Canadian governments necessarily has had to be the form of legislation and regulation of privately-owned financial institutions. Under the British North America Act "the *exclusive* legislative authority of the *Parliament of Canada* extends to all matters coming within the Classes of subjects next hereinafter enumerated; that is to say,—

<sup>14</sup> Currency and Coinage.

<sup>15</sup> Banking, Incorporation of Banks, and the Issue of Paper Money.

<sup>16</sup> Savings Banks.

<sup>17</sup> Bills of Exchange and Promissory Notes.

<sup>18</sup> Interest.

<sup>19</sup> Legal Tender, etc.

Since Confederation, the central concern of the Canadian bank acts of the Federal Parliament has been the exercise of this exclusive authority over such private institutions as create things which are used as the money in Canada.

11. The use of various things as the money of a country is only partly a matter of direct prescription by the law; it is largely a matter of custom within a country. The essential criterion which distinguishes those things which are money from those which are not is the wide or general acceptability in exchange for goods and services or in the settlement of debts. Monetary elements perform simultaneously the functions of being media of exchange and stores of immediately-tradeable wealth. In most countries of the world, Canada included, the main elements of the money stock are, by current custom, bank deposits subject to transfer by cheque. But while things which are money may depend on custom, the monetary and banking legislation of a country and its administration has to regulate directly or indirectly the activities of institutions involved in that creation.

12. Other financial claims can and do perform functions as substitutes for the more traditional elements on a nation's money supply; and some of these may emerge as such close substitutes for currency and chartered bank deposits subject to transfer by cheque that they are virtually indistinguishable with respect to the property of being money. In nearly all the industrialized countries of the world, the debts of institutions which were not regarded as banks have increasingly taken on functions as money, or have become better and closer (if not yet always perfect) substitutes for bank deposits subject to cheque.

13. When and to the extent that debts of financial institutions come to be elements of the money stock, to have a sufficient degree and actual use of wide or general use as a medium of exchange and monetary store of value, then the institutions which issue those debts and permit their ready use in the nation's payments mechanism, are banks. This is so, no matter what their formal titles may be, and no matter what government jurisdiction created the institutions in the first instance. It is operations of the institution that matters and how they are used and regarded by the general public.

14. The fundamental legal basis for the jurisdiction of the Parliament of Canada over the money-creating elements (and immediately related operations) of such institutions (in addition to the chartered banks) is overwhelmingly strong. The four alternatives then are: (i) to require the institutions other than chartered banks to withdraw from these monetary activities; or (ii) to force the institutions engaging in banking activities to obtain a charter under the (federal) bank act; or (iii) to develop some system of integration of and regulation of the money-creating activities of the institutions without requiring bank charters, i.e. without altering the basis of incorporation; or (iv) to ignore the money-creating activities of such institutions, perhaps on the ground that they are insignificant and the risks of mismanagement of their monetary activities are small. The experience with the Atlantic Acceptance Corporation, British Mortgage and Trust and some other financial intermediaries in Canada during the last year and a half have shown the perils of the fourth course. All the other three involve actions by the Federal government, action which would be more clearly formulated and more effectively executed, in my opinion, by defining the primary banking function, along the lines suggested above.

15. To sum up, I believe that the Parliament of Canada should define the primary functions and characteristics of banking, and thus assert the domain of federal jurisdiction. The range and methods of implementation of federal government responsibilities could be adapted, perhaps more narrowly, perhaps more flexibility bearing in mind other activities of the various financial institutions—within this domain. For the bulk of the domain the federal power would be undoubted; at the margins the constitutionality of federal government action could and might be challenged in the courts. Even if such challenges arise, no great harm to the general public or to the public's confidence in an institution need ensue, because the rules applicable to the institutions by virtue of being designated as banks would be more strict—emphasizing greater financial protection for the public—than if the institutions were not regarded as carrying on banking activity.

(ii) *Deposit Insurance; Other Aspects of Integrating Banking Activities in Canada.*

16. Some approach other than a complete and homogeneous integration of all banking functions into a single institutional pattern may be desirable. First, for institutions which carry on limited monetary functions, it may be possible to devise a partial regulation under the federal jurisdiction that will be adequate for the circumstances. The mixture of other banking and financial operations with the money creating and transferring mechanisms may be different from one class of institutions to another. And it may be sensible to bear in mind the heterogeneity of combinations of financial functions in prescribing the law, regulations, channels of contact, institutions and privileges of various institutions which are to some degree in the money-creating business. Within a framework of undoubted responsibility and power of the Parliament of Canada it may nevertheless be attractive to negotiate agreements with the Provinces.

17. A system of deposit insurance, such as has been suggested by the government to accompany the new banks acts, can be a useful procedure for bringing the monetary functions of institutions, in addition to the chartered banks, into an integrated banking network. In my opinion, the federal government has the power to require deposit insurance, without the consent of either the province which incorporated an institution or the institution itself, when the institutions engage in deposit creating and transfer business that is essentially a close substitute for other forms of money. If the definition of banks is developed as suggested above, this would be quite clear.

18. But for deposit insurance to be quite helpful, there will have to be integrated regulations and inspection. Also there will have to be a forward-looking administration of deposit insurance to detect situations of possible trouble before they appear to the public and to facilitate corrections of the troubles. Deposit insurance systems only work well if the insurance provisions have to be used infrequently. In general, deposit insurance will not be sufficient. For the banking institutions to carry out a substantial deposit business and to participate significantly in the payments mechanisms of the country, and to do so safely



from the point of view of the public—it will also be necessary for the whole run of banking institutions to have some indirect or direct routes to the credit facilities of the central bank; and to have adequate access to the clearing system in the country. It seems to me that the Committee should explore all of these relationships very carefully, in studying the prospective relationships between the banking and other financial institutions.

*Interest Rate Ceilings; Scope for Bank Lending and Borrowing.*

19. Bill C-222 applies to the chartered banks in the narrow sense of the enumerated institutions which receive charters under the explicit provision of that act. This would be an extension of the traditional 'special charter' approach to 'banks' in Canada. The remainder of these comments apply to chartered banks only.

20. The draft acts propose the retention of a system of interest rate ceilings until some future time when easier credit conditions arise and when following the application of a formula, interest rate ceilings on general bank lending would cease. While the ceilings continue in operation, the actual levels of the ceiling interest rates will be raised, and will fluctuate as credit conditions vary over a considerable range.

21. In this writer's judgment, it is essential to the interest of the Canadian public in an efficient and equitable financial system and to the efficiency and equity of bank operations for the interest ceilings on bank lending to be raised from the present 6 per cent rate. This is particularly so if the banks are to be permitted and even encouraged to participate in a broad range of borrowing and lending functions in Canada. The substance of the ceiling had been broken in many respects for many years in Canada. Where the ceiling was effective, the main result was to distort the use of borrowing and lending arrangements in Canada. This writer has argued these points elsewhere, particularly in the brief submitted last year and in the article cited above from *The Banker*.

22. The fundamental arguments for removal of the ceilings is that they will be unnecessary and, so long as they exist, a nuisance. The notion is that much more competitive conditions will be created, within the chartered banking community, among chartered and other banking institutions, between banking institutions and other financial institutions, and in capital markets. Much greater disclosure of charges, and in financial operations will also be required. Competition is to be the protector of the public. It may be so, but the deed does not always accompany the wish. This writer can see some merit in the continuation of a system of ceilings on bank lending rates, with different ceilings applicable to each of two or three broad classes of bank lending; and with the ceilings being adjusted by some formula as general credit conditions change. However the extreme difficulties in designing such a system must be appreciated, if it is to be both simple and well-understood, and effective for accomplishing what the ceiling is really intended to do—to act as a check on excessive use of an occasional situation of one-sided balance of financial power in borrowing and lending transactions.

23. Chartered banks are to be permitted an extended range of borrowing privileges under the proposed acts (e.g. borrowing by issuing debentures; markedly reduced cash reserve requirements for time deposits and deposit certificates), and extended range of lending privileges, notably through ability to

participate in conventional mortgages and by greatly improved mortgage lending provisions generally. The alternative to this department-store approach to the range of banking functions is a policy of segregation of various financial functions into specialist institutions—perhaps permitting the banks to create and own satellite bodies to participate in various new or specialized functions. The Australians have gone the latter route. The department-store finance approach seems to this author to be preferable, because it forces explicit recognition of the operations of Canada's banks, whereas the satellite approach makes it very difficult to obtain a properly integrated view.

24. If the competitive position of the chartered banks vis-a-vis other financial institutions is to be improved by the act, then is the competitive position of other financial institutions to be worsened? Which ones? How? The view has been expressed that the positions of the trust and loan companies are to be improved by other means, as well it is hoped, by the development of the deposit insurance system. Presumably the scope of borrowing and lending activities permitted to such companies will have to be enlarged too. Presumably then there is to be some offsetting tendency of improved competitive position of the banks vis-a-vis the trust and loan companies and vice-versa.

25. In this writer's brief on the 1965 Acts he criticised the provisions regarding the scale of charges permitted to chartered banks for inter-branch and inter-city collections; and expressed the hope for a broadening of the base of the clearing house system. This writer stands by the earlier positions he took on these matters, but it may be inexpedient to press these points now. The issues are of lesser significance than the fundamental structure and scope of operations of the banking system with which the Committee must deal.

## DECENNIAL REVISION OF CANADA'S BANKING ACTS

### A PRELIMINARY REPORT ON THE PROPOSED LEGISLATION

(David W. Slater)

*(Reprinted by courtesy of the Canadian Bankers Association).*

On July 7, 1966, the long-awaited legislation to provide the "decennial revision" of the Bank Act in Canada was introduced—Bill C-222. Parallel legislation regarding the Quebec Savings Banks was also introduced and somewhat earlier an Act to amend the Bank of Canada legislation—Bill C-190. These bills were given first reading prior to the summer recess of the House of Commons. In the ordinary course of events extensive committee work on the bills, particularly by the House of Commons Standing Committee on Finance, Trade and Economic Affairs, will take place this autumn. This will include public hearings. Legislative action on the bills as amended then would follow. The Senate too may give the bills extensive consideration, including a study by a Senate Committee. Other financial legislation related to the banking acts may be introduced and considered as part of an integrated revision of Canada's financial arrangements. Legislation to set up a system of deposit insurance has been promised by the Minister of Finance. The financial aspects of Canada's housing legislation and perhaps legislation on trust and loan companies may have to be treated too.

The purpose of this article is to report on the principal changes thus far proposed. It is not the authors' intention to discuss here the pros and cons of the proposals nor to attempt to forecast the parliamentary treatment of them, nor to predict the economic and financial implications of changes which will emerge. Such a course is not appropriate in this column at this time. It should be emphasized that this description, which must select items considered important or particularly interesting, is the author's responsibility; it in no way represents the official position of The Canadian Bankers' Association nor any of its members. A report on the proposed changes may nevertheless help in the appreciation of the discussions expected this autumn; by comparing the proposals with present arrangements; by integrating elements from various bills and statements; by comparisons with other arrangements and proposals; by indicating some of the issues on which judgments may be required.

As background it should be recalled that the Royal Commission on Banking and Finance (the Porter Commission) made a number of recommendations in its Report (1964) to modify the structure and operations of Canada's chartered banks and other financial institutions in Canada. These proposals have been reviewed in this journal<sup>1</sup> and elsewhere.<sup>2</sup>

It will also be recalled that bills to amend the Bank of Canada Act and the bank acts were introduced and given second reading in 1965, but that these proposals lapsed as the bills were not given full legislative treatment before the prorogation of Canada's 26th parliament. The new bills are very like the earlier ones in some respects, e.g. regarding ownership and control of banks and other financial institutions; but quite different in others, notably regarding reserve requirements, the interest rate ceilings, debenture arrangements and in the proposed relationships to deposit insurance.

The major proposals of the Bank Act regarding mortgage credit and interest rates will be discussed first, then the proposals of the various acts regarding cash and secondary reserves and debentures. Proposals to influence ownership, direction and control of banks and the relationships to control of other financial institutions will then be considered with other administrative matters. The proposals regarding deposit insurance are then discussed, and important changes in the Bank of Canada Act. Finally, some of the major issues are indicated.

#### Mortgages, Interest Ceilings, Cash and Secondary Reserves

The broadening of the mortgage lending power of Canadian banks is one of the most important proposals in the new Bank Act. The Canadian banks are to be permitted to lend on the security of "any real or personal, immovable property..." (Section 75), subject to some general (and not particularly) restrictive limitations. It will be recalled that the long tradition in Canadian

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<sup>1</sup>The *Canadian Banker*, Vol. 71, No. 2, Summer 1964 contained articles by Dr. E. P. Neufeld, Mr. J. E. Toten, Mrs. Alison Mitchell and by this writer. Vol. 71, No. 3 Autumn 1964 contained articles by J. A. Galbraith and by this writer.

<sup>2</sup>R. M. MacIntosh, "Chartered Banks at the Cross-Roads", *Business Quarterly*, Winter 1965; F. H. Schott, "Report of the Canadian Royal Commission on Banking and Finance: A Review", *Monthly Review of the Federal Reserve Bank of New York*, 6 August, 1964; J. C. Weldon, "Women Preachers and The Porter Commission", *Queen's Quarterly*, Winter 1965; J. F. Chant, "The Porter Commission on Canadian Banking and Finance", *Quarterly Review of the Banca Nazionale del Lavoro*, June 1965; David W. Slater, "The Report of The Royal Commission Banking and Finance", *Canadian Journal of Economics and Political Science*, August 1965; Herbert Stein, "Report of the Royal Commission on Banking and Finance, 1964: Review Article", *The Journal of Political Economy*, June 1966.



banking, which prohibited lending on mortgage security, subject to only a few exceptions, was first modified significantly in the Bank Act of 1954. That act permitted the banks to lend on the security of insured National Housing Act mortgages. Banks were not permitted to enter the conventional mortgage business for newly-constructed or existing property.

The new Act proposes that the banks be allowed to carry on the whole range of mortgage lending subject to limitations on the percentage loan to security valuation in single mortgages and on a bank's total holdings of residential mortgages. For NHA insured mortgages, on a single mortgage the bank may lend such percentages of value of the property as are prescribed in National Housing Act and its administration. Nowadays the NHA mortgages generally run in the range of 83 to 90 per cent of the value of the property but they apply only to newly-constructed housing. For conventional mortgages the new Bank Act proposes that "the amount of the loan or advance shall not be more than seventy-five per cent of the value of such property..." (Section 75). The new Bank Act places no limits on the total NHA insured residential mortgages that a bank may hold, but does limit the total principal amount of conventional mortgages on residential property to three per cent of Canadian deposit liabilities and outstanding debentures of a bank at the outset, increasing one per cent per annum to reach a maximum of ten per cent. The broadened mortgage powers for Canada's banks, when taken in association with the proposed changes in interest ceilings, imply that the banks are expected to take on a major enduring role in both the NHA insured and conventional mortgage lending activities in Canada. In a more profound sense, the implication is of broadening rather than narrowing the combination of functions carried on by Canada's chartered banks.

Another major change in the acts concerns the ceiling on interest rates on bank loans. It is proposed that the present Act's six per cent ceiling is to be replaced in the first instance by an adjustable maximum, the adjustments being made according to a formula as the average of the market yield on short term bonds of the government of Canada changes. In general terms (subject to many technical details about various implementation and adjustment procedures) the maximum interest rate that is proposed is  $1\frac{3}{4}$  per cent per annum above the average of the market yield on the short bonds. If the early August 1966 yield on short Canada bonds (almost 5.5 per cent)<sup>3</sup> ruled at the time of the implementation of the proposal, for example, then the maximum interest rate on bank lending would be  $7\frac{1}{4}$  per cent per annum. This maximum would apply to the general lending activities of the bank except (according to Sec. 91 (6)) those based on mortgage security. It should be recalled that the maximum interest rate on NHA insured mortgages was  $6\frac{3}{4}$  per cent in the summer of 1966, and conventional mortgage rates were in the range of  $7\frac{1}{2}$ -8 per cent.<sup>4</sup> The proposals in the Act imply the retention of a ceiling system for an indefinite period in the future, (the Act's provisions for removal of the ceiling are discussed below) probably some increase in the ceiling from present levels at the time of implementation of the Act if the proposal is implemented in the next few months, (because it is inconceivable that credit conditions would ease so much so quickly) and an adjustment of the ceiling from time to time as credit conditions tighten and ease. Nothing in the Act indicates that the present *system* of terms of

<sup>3</sup>Bank of Canada, *Weekly Financial Statistics*, 4 Aug., 1966.

<sup>4</sup>Financial Post, 6 Aug. 1966 reports the range as  $7\frac{1}{4}$ -8 per cent.

lending by the banks on personal loans is to be altered. Indeed the Minister has pointed to the beneficial effects of the development of bank programs of personal loans.

The proposed Bank Act provides for the *removal* of the ceiling on interest rates on bank lending if significantly easier credit conditions emerge in the future. In general terms the ceiling is to lapse if and when the average interest rate of short Canada bonds falls to the level of four and a half per cent,<sup>5</sup> i.e. if and when the adjustable ceiling on interest rates on bank lending has fallen to six and one quarter per cent. If the ceiling is removed by such a procedure and event, the proposed Act does not call for reimposition of the ceiling if credit conditions tighten thereafter.

A third set of important changes concerns cash reserves and secondary provisions applying to the Canadian banks, the new proposals appearing partly in the Bank Act and partly in the amendments to the Bank of Canada Act. Under the present arrangements, all Canadian dollar deposit liabilities of the banks are subject to a uniform cash reserve requirement. The Bank of Canada is permitted to designate a cash reserve requirement. The Bank of Canada is permitted to designate a cash reserve ratio in the range of 8 to 12 per cent. The rate has never varied from 8 per cent under the 1954 acts, the Bank of Canada never having used its power to alter the minimum. (Officers of the Bank of Canada have indicated on several occasions that the power to vary the minimum was regarded as an instrument to be used in emergencies, rather than as a routine vehicle of monetary policy). Cash under the present system consists essentially of Bank of Canada deposits and Bank of Canada notes owned by the banks. The minimum cash requirements are calculated by a ratchet formula by which this month's cash requirements depend on the minimum ratio specified, and last month's deposit liabilities. No legal power has existed to require the chartered banks to hold secondary reserves, but the chartered banks agreed with the Bank of Canada in 1956 (and continuously thereafter) to hold a combined total of cash plus certain liquid assets amounting to at least 15 per cent of the deposit liabilities.

On the surface great changes are proposed in these arrangements in the new acts. Minimum cash reserve ratios are to be fixed by the Bank Act, the ratio not being subject to variation at the discretion of the Bank of Canada; a 12 per cent minimum to apply to demand deposits and 4 per cent to deposit liabilities payable after notice. Banks are to be legally required to hold secondary reserves, with the Bank of Canada being given discretion to set the ratio at zero or to vary the minimum secondary reserve ratio in the range of 6 to 12 per cent of Canadian dollar deposit liabilities of the banks. Bank debentures, about which more is said below, are to be free from legally required minimum cash reserve ratios.

The proposed reserve changes for Canada's banks are not as great as they appear at first sight. Given the present distribution of the bank deposit liabilities the average cash reserve requirements are apparently to be reduced from the present 8 per cent to something approximating 7 per cent. The average in the future would, of course, depend on the future development in the distribution of

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<sup>5</sup>Short Canada bond yields were below this level generally in 1963 and for part of the year 1964, as well as in 1961 and 1962, except for a few months after the exchange crisis.



bank liabilities. The level of minimum secondary reserve holdings, which the Bank of Canada may require, within the proposed 6 to 12 per cent range, is not clear. If it is less than 8 per cent, the overall cash plus liquid assets requirements on the Canadian banks would be eased a little by the new acts, both by reducing the total ratio required and by permitting a smaller proportion of the total to be held in the form of cash (which yields the banks no interest under the Canadian system). The ratchet system of adjusting the bank cash reserve requirements is to continue with the difference that the calculation is to be on a semi-monthly rather than a monthly basis. This change to a twice-monthly calculation will tend in practise to increase the amount of cash a bank must hold and will offset, to some extent, the reduction in the legal requirement. The acts contain various technical provisions to smooth the transition from the existing reserve requirements to the new ones, so that no major shocks to the financial system should accompany the changes.

The purpose of the adjustments in the cash reserve requirements is, according to the Minister, to establish more desirable competitive conditions between the banks and other financial institutions, particularly in notice deposit, term deposit and debenture activities. The imposition of legally-required secondary reserve provisions and the shifting of the Bank of Canada's discretionary margins from cash to secondary reserve requirements are technical changes in the instruments of monetary management available to Canada's central bank. Their future significance is unknown; it depends on the use which is developed for the new instruments. It seems probable however that variations in the minimum secondary reserve ratio may be a more significant element in the ordinary management of monetary policy in the future than has been the discretionary power which exists at the present time.

As noted above, the banks are to be empowered to issue "bank debentures", a form unsecured indebtedness of a bank which, according to the proposed act, must have a stated maturity of at least five years after their date of issue at the time of issue. Under the proposal the total amount of such debentures which a bank may have outstanding is limited to one-half of the total of the paid up capital stock and rest account of the bank, a maximum reached after an initial period in which the limit is raised ten per cent each year. The intention of this provision is clearly to enlarge the scope of intermediary functions of the banks by permitting them to borrow for longer terms and presumably also lengthen the average term of their lending. This development is, for example, consistent with a marked enlargement of the role of banks as mortgage lenders.

#### Control and Competition of Banks and Other Financial Institutions

Bill C-222 proposes quite a large number of major changes in the control or administrative arrangements permitted within banks, among banks, and between banks as a group and other institutions. A person is not to be eligible to be elected or appointed a director of a Canadian chartered bank if he is a director of another Canadian bank or if he is a director of a trust or loan company. (The latter provision will apply after the interest ceiling on bank loans lapses, and it will be subject to transitional arrangements.) He is not to be allowed to be a director of a bank if he is also a director of a holding company which in turn has a significant degree of control or influence in the affairs of a trust or loan company. Limits are placed on the proportion of directors of a Canadian corporation who may be directors of any one bank. Canadian banks are to be



restricted to not more than a 10 per cent equity position in other companies apart from certain limited exceptions, namely the Export Finance Corporation and what are specified as bank service corporations. Subject to certain provisions for a transitional period, banks must divest themselves of holdings of equity positions in other companies in excess of the modest proportions which will be permitted under the new Act. Governments are not permitted to acquire equity positions in Canadian banks, although provisions are made whereby government pensions and other funds may make investment in non-voting bank stock.

In introducing these proposals the Minister of Finance indicated that they were directed toward increasing the degree of competition in the Canadian system of banking and finance. The acts also propose to prohibit agreements among banks on interest rates on both loans and deposits. Mergers of banks will continue to require the approval of the government. Banks are to be required to provide somewhat more comprehensive public information on their operations and positions, including the valuation reserves on their assets.

One of the other major proposed changes in ownership, control and operations of Canadian banks concerns the position of foreign residents. Foreign residents are to be limited in their ownership of shares in any Canadian bank, essentially by limiting the total foreign ownership in any bank in the future to a maximum of 25 per cent of voting shares. A bank in which more than 50 per cent of the shares were owned by one non-resident shareholder in September, 1964, would be exempted from this provision. Various provisions are made to limit the transfer of shares to foreign owners (or to Canadians under the ten per cent limit mentioned below) to insure that these provisions are not circumvented by trustee arrangements, and actually to prohibit the transfer of share ownership under certain circumstances. Banks are permitted to limit foreign participation in any new share issues, including those distributed through systems of rights. Moreover, in the future any single person, corporation or similar body, (or associated persons) Canadian or foreign, is to be limited to a maximum ownership of ten per cent of the outstanding shares of a Canadian bank. Rules are also proposed to limit the size of total liabilities in relation to the authorized capital of any bank which is more than 25 per cent owned by one shareholder or related group. This provision would apply to the one chartered bank which is now foreign owned and controlled.

In the statement at the resolution stage of the new Bank Act, the Minister of Finance indicated the intention of the government to establish a crown corporation to implement a system of deposit insurance in Canada. The draft bill was not introduced before the summer recess and therefore the description of the proposed system and of most of the relationships of that system to the other parts of the legislation will have to be postponed to a later article. In his statement on the Bank Act resolution the Minister indicated a number of points of great significance about the intended deposit insurance system.

The intention appears to be to have the system comprise banks and other federally-incorporated deposit taking institutions which would be required to join; provincially-incorporated deposit taking institutions may join if the institutions and the provinces desire deposit insurance. The system of deposit insurance will require effective inspection and adequate regulation and, therefore,

federal provincial agreements may have to be worked out to cover the provincially-incorporated institutions, even if it was pretty much left to the institutions to decide about coming in or staying out of the system.

One deposit insurance crown corporation is proposed, not two. It is not yet known whether the proposals envisage the banks and the "near-banks" being dealt with by a single system of rates, presumably with a uniform set of insurance rates applicable to all institutions, or whether different insurance rates may apply to different classes of institutions. Provincially-incorporated institutions are apparently not to be required by the federal government to insure their deposits. It is not clear whether some provinces might *require* some of their incorporated institutions to participate in the Federal insurance, or whether the arrangement would be optional to all provincially-incorporated institutions. Apparently, a provincially chartered institution when it wishes to opt into the federal deposit insurance scheme must have approval from the provincial government which incorporated it.

#### Proposed Amendments to the Bank of Canada Act

The most important thing to say about the amendments of the Bank of Canada Act, is that most of the proposed changes are rather minor. The two main items concern: 1—the relationship between the government and the Bank in regard to monetary policy; and 2—the legal provision regarding cash reserve and secondary reserve requirements for the chartered banks and Quebec Savings Banks. The latter has already been discussed in this article; the former now requires attention.

Views have changed from time to time about the relationship between the government and the Central Bank in regard to monetary policy; different positions have been taken on these matters in various parts of the world. Almost everywhere, however, the directors or chief officers of central banks have been given some degree of independence from government direction (and therefore responsibility) in the management of monetary policy. These limited degrees of independence have to be integrated in a meaningful and effective way into general government responsibility for economic policy and a variety of devices have been used in different countries. Canada's arrangements have changed from time to time since the establishment of the Bank of Canada in 1934. They are now a somewhat complicated maze of legal positions, ministerial assertions, statements of understandings by responsible persons—arrangements which have been only partially tested in practice.

The locus and machinery for controlling monetary policy are to be clarified in certain respects in the proposed amendment to the Bank of Canada Act. The relevant passages in section 14 are:

- (1) The minister (of Finance) . . . and the governor shall consult regularly on monetary policy and on its relations to general economic policy.
- (2) If, notwithstanding the consultations provided for in subsection (1) there should emerge a difference of opinion between the minister and the Bank concerning the monetary policy to be followed, the minister may, after consultation with the governor and with the approval of the Governor-in-council, give to the governor a written directive concerning monetary policy, in specific terms and applicable for a specified period, and the Bank shall comply with such a directive.



Provision is made for publication of the directives.

The old arrangement whereby the governor could veto the actions or decisions of the board of directors or the executive committee of the board of directors (a board which was appointed by the Governor-in-council in the Cabinet; the executive committee included the deputy minister of finance as a member *ex officio*) is to be repealed. It may be recalled that under this provision the governor was required to inform the minister of Finance of a veto and that various provisions were made whereby the minister had to submit the veto, confirming or disallowing, to the Governor-in-council; various provisions were also made whereby directors or members of the executive committee could inform the minister of their views and these views were to be transmitted to the Governor-in-council. These arrangements were part of the old procedure whereby the degree of independence of the governor was established but made conditional on the ultimate power of the government.

At several other places in the proposed amendments minor provisions are also made which clearly establish the responsibility of the government for the basic policies of the Central Bank. However, the Act, even as amended, still has a very strong implication that the Bank should have a substantial degree of independence in monetary policy. It is not proposed to alter the conditions of appointment and tenure of the governor of the Bank of Canada, conditions which are much like those applicable to a judge except that the governor is appointed for a limited term (reappointment is permitted). The principal way in which the government will influence monetary policy is by a development of common views and consensus between the Cabinet, acting through the Minister of finance and the governor. The provision regarding directives is a formal one which may almost never be used. It is unlikely to be used as an ordinary part of the management of monetary policy.

The remaining changes proposed in the Bank of Canada Act are of a rather minor nature, with perhaps one exception. Provisions are made to ensure that the directors of the Bank of Canada have no material interest in the control or direction of chartered banks. The requirements of the Bank of Canada to state its bank rate are set out a bit more clearly. Various minor provisions are made to deal with the Bank of Canada's handling of small inactive deposit accounts of chartered banks that have been turned over to it by the chartered banks. The only provision that may have considerable significance is a broadening and generalization of the power of the Bank of Canada to accept deposits from other central banks and other international financial institutions and to pay interest on these. This may have some significance in the developments in the international monetary system. Cooperative arrangements among central banks, national governments, and international institutions may make it attractive to develop a considerable international deposit business at the official level, *with interest payments*. The Bank of Canada will be formally authorized to engage in such arrangements, if and when the Amendments to the Bank of Canada Act are adopted.

Diehard believers in the older gold standard arrangements will feel at least a little twinge at the formal abandonment of reserve requirements for the Bank of Canada itself, requirements which have not operated for many years.



### Federal-Provincial Relations Regarding Financial Institutions

Does the federal government have the power to regulate the "near-banking" activities of provincially-incorporated institutions? Even if it does have the power, may it be attractive to work out cooperative systems of regulation of financial institutions and practices with the provinces? What regulations are required and for what reasons? What are the relationships between regulations of banking and near-banking activities and operations of other financial institutions? These questions of financial legislation in a federal state are among the most important and difficult to resolve; the legislation proposed and the statements concerning it indicate some of these difficulties. The intention here is merely to indicate some of the difficulties and points of view.

One view is that the federal government has the power to regulate a considerable range of the "near-banking" activities of all institutions, both federally and provincially incorporated, without any agreement or permission being granted from the provinces. The range includes deposit business (subject to cheque or easy liquidation at the issuing institution), i.e. the creation of money or near-monies that are close substitutes for money, and substantial active participation in the country's payments system. This view is based fundamentally upon the federal government having the sole constitutional rights in matters of banking and currency; but the federal government's constitutional position is supplemented, according to some views, by its rights to regulate interest and the general constitutional provisions under the commerce clauses. According to these views, the regulation of banking activities is an entirely separate issue from the question of which government incorporated a financial institution. If an institution opts into banking and currency functions, interpreted in a realistic modern sense, then these views suggest that the federal government can apply such regulations of these functions as it sees fit. If it wishes to *require* institutions to participate in a deposit insurance system or other banking regulation it may do so, without the consent of the provinces. If it wishes to make deposit insurance or other arrangements available *on a voluntary basis* to provincially-chartered institutions according to this view it can also do so without consent of the provinces.

Quite different notions of the federal government's constitutional position regarding banking and currency activities are held by other knowledgeable and responsible people. Some take the view that the federal government is supreme in matters of banking and currency, but the range of institutions and activities to which these powers apply is a rather narrow one, not including what are sometimes called near-banking activities of provincially incorporated institutions. Others point out that the Federal Parliament does not have the unquestionable right to designate what it will call banking activities, and thus the unquestionable right to extend its constitutional powers over banking to a broad range of activities. It is argued that judicial reviews and tests will be required of unilateral federal actions to extend regulations or make privileges available to provincially-chartered institutions and some people doubt the liberality of the decisions that would likely follow. Doubts are expressed also about federal powers in regard to provincially-incorporated financial institutions under *other* sections of Canada's constitution. While conceding that the situation is uncertain, other people argue that the Federal government must take a strong initiative in defining and taking responsibility for banking activities, subject of course to

challenge and modification by judicial processes. In discussions of Bill C-222, the Minister of Finance and others have taken the limited view of federal powers over banking but some speakers have already expressed judgements that Federal powers and responsibilities for banking are large.

Whatever may be the constitutional position regarding the powers of the federal government over banking and "near-banking," many people feel that co-operative arrangements between the federal government and the provinces in the regulation of financial institutions are highly desirable. Many individual institutions are engaged in banking *and* other activities, and it is difficult to separate the activities in all important respects. Thus regulations of banking activities of provincially incorporated institutions would affect the non-banking activities, many of the latter lying within provincial jurisdictions. Interdependencies exist between banking and non-banking problems, even when these are carried on by distinct institutions, or can be separated quite effectively within a particular institution. For example, if an adverse report was made on the banking activities of a provincially incorporated institution, the institution's non-banking activities would probably also be influenced.

The statement of the Minister of Finance at the Resolution stage of the Bank Act expressed at several points and in several ways the desirability of federal-provincial co-operation in the regulation of financial institutions. He said:

As part of the long term policy to promote competition and flexibility in the financial system, it is desirable that *progress be made in the legislation governing all financial institutions, both federal and provincial, and that the measures taken in regard to the various classes of institutions should be related to one another in such a way as to achieve the broad objective.*<sup>6</sup> Already we have done this in considerable measure in regard to our federal institutions and I expect that we will be able to carry the process further, not only in our banking legislation and our legislation relating to trust and loan companies and insurance companies but also in subsequent legislation regarding corporations and related matters, especially with regard to the disclosure of information.

Officials of the federal and provincial governments have recently met to discuss these and related matters. Out of this activity at both levels of government will come, I trust, a broadly integrated approach designed to improve our financial system as a whole so that it can better serve Canadian individuals and Canadian business.

The Minister's statement also referred twice to his initiative to develop a federal-provincial meeting on the important subject of consumer credit and interest disclosure. The proposed deposit insurance corporation, as has been noted above, is to "be authorized to insure the deposits of provincially-incorporated institutions where this was desired by the institutions and the provincial government concerned. *The government will discuss this matter with the provincial authorities.*" Other indications of cooperative federal-provincial approaches have been given. Constitutional and cooperative arrangements between the federal and provincial governments are probably the most important and difficult background issues in the revision of the Bank and related acts.

<sup>6</sup> Italics added.

## THE 1965 REVISION OF THE CANADIAN BANKING ACTS

A Review and Comment on some Features of Bills C-102,  
C-103 and C-101, First Reading 6 May, 1965

(by David W. Slater, Queen's University, 31 May, 1965)

These comments are intended as a small contribution toward the current revision of the Canadian banking acts. The principal interest is in Bill C-102, the proposed new Bank Act.

In a number of important respects this bill appears to require reconsideration and revision. Some of its provisions are quite unsatisfactory, including:

the regulation of interest rates on bank lending; the scale of charges permitted for inter-branch and intercity collections; and, the rigidities introduced into bank operations in mortgage lending.

In other respects the bills appear to be deficient in not dealing with certain fundamental issues, or in dealing with them in a very ambiguous manner, including:

the control and terms of operation of the clearing house system; the competitive position and controls over banks and their "near-competitors"; the principles of monetary policy implied by the proposed statutory system of variable minimum secondary reserve ratios.

Most of what follows is critical of the proposed bills. It is appropriate therefore to record, at the outset, one's applause for a number of the proposed innovations and to hope that they are accepted by Parliament. In my judgment the very good features of the new Bank Act include:

the reduction in ownership (and presumably also in control) by banks over other corporations, including trust and loan companies; the prohibition of agreements between banks on lending and borrowing rates; the proposed limitation on the ownership and control of banks by Canadian governments; and the encouragement of the banks to engage more in mortgage lending.

The bills invite comparison with the Report of the Royal Commission on Banking and Finance (the Porter Commission). In my judgment the comparison is rather unfavourable to the bills—with respect to the appreciation of financial evolution, and in clarity, imagination, balance and analysis. However it appears pointless to argue such generalities now. Thus most of what follows is directed to specific points included in or omitted from the draft legislation. References to the Porter Commission are selected accordingly.

*The 6 per cent Ceiling on Interest Rates on Bank Lending*

Subject only to specific exceptions for NHA mortgages and under certain conditions for conventional mortgage lending (Section 77), the proposed revision of the Bank Act retains the old maximum of 6 per cent per annum as a charge for bank loans or advances payable in Canada (Section 91). This is a very unsatisfactory feature of the act; indeed its retention is seriously misleading in some respects and distorting in others. Such an interest ceiling can only provide illusions of controlling the general or average level of credit terms in the country. A realistic system of interest ceilings might, at best, provide some protection of the public against financial institutions taking advantage of special



bargaining positions. But the provision drafted in Bill C-102 is incapable of even contributing to such an end, because it is so completely unrealistic.

In two important respects, the substance of this ceiling on interest rates for bank lending has been breached for many years, and presumably is to continue to be breached. Banks can and do buy securities, including new issues of municipal, provincial and industrial bonds to yield gross interest returns in excess of 6 per cent per annum. Putting aside fine legal distinctions and dealing with the real essence of the matter, such practices clearly involve the banks making loans at interest rates in excess of 6 per cent per annum. Moreover, a large fraction of the consumer instalment financing which is carried out by the Canadian banks is at effective gross rates of interest well in excess of 6 per cent per annum. The fact is only thinly-disguised by systems in which repayments of such loans are placed into a deposit account which is credited against the outstanding amount of the loan only when it cumulates to the whole principal of the loan. Presumably the banks are to be permitted to continue to engage in consumer installment loan business; and if so, they will have to be permitted, by some devices, to charge more than six per cent per annum gross rates of interest on the amount outstanding of such loans.

The primary effect of the six per cent ceiling on rates of interest in bank lending is now to distort the use of borrowing and lending arrangements in Canada. With contemporary economic circumstances and policies in the world, the interest rates on Federal Government bonds in Canada are often in excess of 5 per cent per annum. These securities carry minimum risks and involve extremely low costs of administration to the investor. When this is so, most classes of borrowing and lending (which involve significant risks, administrative costs and perhaps illiquidities) will only be competitive at gross interest rates which are significantly higher than the yields on government bonds. For some loans, interest *premiums* of  $\frac{1}{2}$  or 1 per cent per annum above government bond rates will do; but for some gross interest *premiums* of 3, 4, 5 per cent and more, above the gross yields on government securities will be required to make lending competitive. Banks are expected to, and they certainly should be participating in classes of lending activity in which significant costs of administration and risks arise. To the extent that they are limited by a 6 per cent maximum gross interest rate, lending and borrowing arrangements will be distorted in the country, in many ways.

In the first place, the six per cent ceiling only applies to certain kinds of bank lending. One effect of the ceiling therefore is to drive the banks out of the classes of business to which the ceiling applies and into the kinds of business to which it does not apply. Secondly, for various reasons, the banks may continue to do some business with the customers and in the forms to which the ceiling applies; but they will ration the business they do on these terms. Moreover, they will almost inevitably be encouraged to find devices to get around the ceiling, for example by pressuring customers to hold increased average deposit balances in the banks, to use time notes instead of demand notes, and so on. Thirdly, many customers will be driven into the hands of other lenders who are not subject to such a ceiling. It is possible that the ceiling will weaken the competitive position of the banks to attract deposits, thus tending to diminish the lending business by the banks which are subject to the ceiling and expanding the lending business of other institutions which are not subject to such ceilings. The 6 per cent ceiling is

thus partly an illusion and partly a distorting influence in general credit terms in the country.

According to a report (Globe and mail, International Edition, *Report on Business*, May 10, 1965) of a press conference of the Minister of Finance, the government rejected the Porter Commission recommendation to remove the 6 per cent ceiling because it would have been contradictory to government policy to keep interest rates in Canada down. This argument will not do. It clearly is government responsibility to influence the level of interest rates and general credit conditions in Canada. But the 6 per cent interest rate on bank loans makes no contribution whatsoever to the level of interest rates and the general or average state of credit conditions in Canada. At most the ceiling provides some illusions in this regard, by keeping the interest rate on certain classes of lending down. But other elements of credit conditions on such bank lending are tightened; and lending is switched to other channels and arrangements. Indeed, under not-all-that-unusual conditions, the effect of the interest ceiling on bank lending in Canada is to make the general or average terms of borrowing in Canada tighter than they would be without the ceiling.

Thus general credit policy provides no support for retention of the 6 percent ceiling. The ceiling as it now stands is detrimental to the efficient operation of borrowing and lending arrangements in Canada. In its present form it makes no contribution to the equitable organization of lending arrangements. The government acquiesces in higher rates on some bank lending. It tends to mislead the Canadian people. The case for removal of the ceiling is overwhelming.

A case may be made for including a realistic set of interest rate ceilings in Canada's financial legislation. The essence of this case is that the country cannot always count on competitive financial arrangements protecting the public. Situations may arise at various times and under various circumstances in which financial institutions have a peculiarly strong bargaining power in relation to certain classes of transactions. Imperfect markets and competitive structures may then lead to financial institutions taking advantage of such events. Some system (interest ceilings are only one of the alternatives) for protecting the public against these possibilities can be justified. If interest rate ceilings are to be used for these purposes, then they have to be realistically structured; they must be capable of doing what they set out to do. Results ought not to be expected of them that they are incapable of yielding. A number of ceilings of increasing height will be required, each to apply to various broad classes of lending which differ in risk, in cost of administration and in liquidity to the lending institution. For some classes of business the ceiling on gross rates of interest might be 7 per cent, and for other classes of business, 9 per cent and so on. Clearly also some sort of scheme of reviewing and adjusting these ceilings will be required as the general credit conditions ease or tighten. Such adjustments might be tied to major changes in interest rates on government securities.

#### *Charges on Discounts*

Section 92 of the New Act retains the old arrangement by which banks may, in discounting a bill of exchange, promissory note or other negotiable instrument, in order to defray the expense of collection thereof, charge in addition to the discount thereon:

- (a) where the instrument is payable at a branch of the bank of Canada and is discounted at another branch, an amount not exceeding one-



eighth of one per cent of the amount of the instrument or fifteen cents, whichever is greater, or

- (b) where the instrument is payable at a place in Canada, other than a branch of the bank, an amount not exceeding one fourth of one per cent of the amount of the instrument or twenty-five cents, whichever is greater.

*This section encourages the retention in Canada of the present unsatisfactory scale of charges for inter-branch, inter-city and inter-bank clearing. This system distributes the costs of banking operations inequitably. It perpetuates the non-par clearance system in Canada. It can discriminate against the smaller regional banking-type institutions. It appears to run against the considered judgement of the Royal Commission on Banking and Finance on this matter. At p. 394 their Report states:*

We also recommend that there be a statutory prohibition on charges for the negotiation of out-of-town cheques, the actual handling of which does not involve any significant extra cost to the institutions concerned.

A case can be made for bank customers paying specifically and directly for the various services rendered to them. Within such a framework, which would rule out par-clearance of negotiable instruments settled at a distance, customers would bear directly the genuine collection costs of clearing inter-branch, inter-bank, inter-city transactions. But even so, the scale of charges which are permitted (encouraged may not be an unfair term) by Section 92 of Bill C-102 would be objectionable. The genuine collection costs of clearing a large inter-branch, or inter-bank, or inter-city payment are not more than for a small one. If the genuine extra cost of clearing an inter-city cheque of 100 dollars is 15 cents, this is also the extra cost of clearing one of 1000 dollars or 1,000,000 dollars. The same is true of other bills of exchange, promissory notes or negotiable instruments. The permission for scaling the charges as a per cent of the amount of the instrument should be eliminated from the act.

Some bankers used to argue that the collection costs should reflect the fact that the person discounting the bill received his proceeds on one day and the bank received its proceeds only two, three or more days later, after the process of inter-city clearing had been carried out. This was advanced as the justification of the per cent scale of charges. In the aggregate, which is the only proper way to regard this issue, such an argument is completely unsatisfactory. It is one of those notable examples of an argument that appears to be satisfactory when applied to an individual transaction, being essentially wrong when applied to the mass of transactions. While a bank is making payments before it gets receipts from another bank, the other bank is making payments before its receipts from the original bank. The items in transmittal cancel out against one another. Neither of the banks has more nor less cash reserves, more nor less "lending-capacity", because of the delay in settlement of individual items than if the clearing was instantaneous. Therefore there is no interest cost in the aggregate associated with the float in the clearing system. A minor qualification has to be made for net swings in the clearings between one bank and others, but that qualification is extremely minor when the swings to and fro among the banks are averaged out over time.



Quite a good social and economic case can be made for a system of par-clearance of out-of-town cheques, such as exists in the United States. Admittedly it runs against the preceding assumptions that, in the narrow and direct sense, individuals ought to pay specifically for the services rendered to them. But against this point a general consideration must be put; this is of the contribution which par-clearance makes to improving competition between regions and financial institutions and the encouragement to the general economic efficiency of a society. Even if par-clearance is not accepted at this time in revising the banking acts, the provisions of section 92 should be altered: to remove the permission for charges scaled by percentage of value; and to limit a scale of flat charges per item to a clearly-established set of "extra costs" per item.

### *Rigidities Introduced Into Mortgage Lending*

While the proposed Bank Act is to be commended for facilitating the return of the chartered banks to NHA mortgage lending and for introducing the opportunities for banks to engage in conventional mortgage lending, some of the mortgage provisions in the act appear to be overly rigid, others are difficult to relate to the general developments in mortgage finance. The provision in section 77(3) regarding the limited proportion of the deposit liabilities of the banks that can be employed in conventional mortgage lending should be seriously re-examined. So should the provisions regarding exemption of the banks from the 6 per cent interest ceiling on mortgage lending.

The scope of the banks in the mortgage lending business must be examined within the general framework of mortgage finance in Canada, one approach which was set out in the Report of the Royal Commission on Banking and Finance. Is the general Canadian policy regarding mortgages to be, as the Porter Commission recommended, a relative shift away from NHA mortgages (and particularly NHA direct lending) toward a rapidly-improving conventional mortgage arrangement in Canada? Also toward a relatively greater dependence on private lending institutions for NHA financing? Is this to be part of the strategy of improving the use of the existing housing stock in Canada, a problem which is at least as urgent as the provision of new marginal additions to the housing stock in Canada? If conventional mortgages are to be relied on increasingly and, for NHA mortgages, private lenders are to be relied on increasingly, what institutions and arrangements are able to provide adequately and efficiently for these kinds of borrowing and lending? I believe that the restrictions on bank mortgage activity proposed in Bill C-102 are much too rigid in the light of such considerations. Why should the banks be subject to special restrictions on their mortgage lending anyway, when they are considered perfectly capable of disciplining themselves in other kinds of lending? Given the very bad record of forecasting of the developments of housing and mortgage finance during the past decade, how can much confidence be placed in the government's judgement about the sensible boundaries on bank mortgage lending for the next decade? If limits are to be placed on bank lending in conventional mortgages, why must they be related to the general mass of deposit liabilities? Why not give to the Canadian banks the privilege of developing special kinds of borrowing arrangements from the public which are well-suited to conventional mortgage lending by the banks, with permission to employ much larger fractions of such borrowings into mortgage loans.

Bank interest rates on NHA mortgages do not raise unique banking issues; the whole NHA scheme has to be considered in this respect. But there are special provisions in Bill C-102 about exemptions from the 6 per cent interest ceiling on bank loans, applying to bank lending on conventional mortgages. These do raise issues that need to be reconsidered specifically in relation to the Bank Act.

Under the proposed bill, a bank is to be permitted to charge any interest it can obtain on conventional mortgage loans, providing that the amount of the loan is not more than three-quarters of the value of the property on which it is secured, and providing that certain other conditions about term and security are met. What will happen if the bank wishes to make a loan in excess of three-quarters of the value of the property? Presumably it could do so, only if the interest rate on the whole loan was less than or equal to 6 per cent per annum. But if conventional mortgage rates are in excess of 6 per cent, what would then happen? Either the bank would not make loans in excess of  $\frac{3}{4}$  of the value of the property, much too low a percentage for modern Canadian conditions. Or else, borrowers, banks and other institutions will be encouraged to find various, more or less unsatisfactory devices, to get around the restriction. The relationships that are to be permitted between bank conventional mortgage lending and some of these other, already existing, arrangements is by no means clear. Is a bank to be permitted to enter into a consortium with other institutions, using various instruments (including blended first, second and third mortgages and other instruments) to collectively make loans to a value more than  $\frac{3}{4}$  of the value of the property? Would the banks then contravene section 77(2) by so doing?—sometimes?—under what circumstances?

#### *The Control and Terms of Operation of the Clearing House System in the Payments Mechanism*

The system of inter-branch and inter-bank clearing, the heart of the operation of a modern payments mechanism, has been under the control and management of the chartered banks in Canada for many decades. The right to operate this clearing system was delegated by the Canadian Bankers' Association Act to the Association many decades ago. The central questions of control concern the terms of settlement at clearing (when and how institutions must settle) and the charges imposed on institutions for the use of the clearing facilities. Over the years the operators of the clearing house have permitted certain institutions other than the chartered banks (the Quebec Savings Banks, and some trust and loan companies) to use the clearings system. The Royal Commission on Banking and Finance recognized the possibility that the chartered banks who control the clearings system could manage it in a way that discriminated against their (now-marginal) competitors in the payments mechanism. But the Commission did not believe that such discriminatory practices had arisen. For example, in referring to the competition between trust and mortgage loan companies, they said: (p. 182)

We were told that some (trust and loan) companies have stressed their non-chequable deposit business because they do not like to rely too heavily on chequeable accounts for which they must apply to the chartered banks for clearing arrangements. It must be stressed that this is mainly a reflection of vague fears about the future, and not of difficulty experienced to date.



It may be recalled that the Porter Commission recommended that the control over the clearings system be shifted from the present manager, the Canadian Bankers' Association to a newly-constituted, broadly-defined group of banking institutions, which would include all those financial intermediaries engaged in short-term borrowing from the public. The Commission's recommendations on clearing were partly related to the application of their broad concept of banking institution and the uniform cash reserve rules that they recommended for all such institutions. But even if the banking acts before the House of Commons do not embody these ideas, the modification of the clearing system in Canada should be considered.

It seems inevitable that the provision of banking services in Canada will become more diffused among a variety of kinds of financial intermediaries. If so, regardless of other institutional changes, should not all of the participants in banking business (in the real economic sense of that term) have rights and responsibilities in the clearings system? May not the time have thus been reached for statutory provision of the broadening of the control of the clearings system? Perhaps provision should be made formally to require non-discriminatory, non-arbitrary terms of settlement for all items that may enter into the payments mechanism. Perhaps some supervision of the clearings system to this end should be introduced, e.g., through the Inspector-General of Banks.

#### *Banks and "Near-Banks"*

The Porter Commission's ideas and recommendations on competition and regulation of the chartered banks *and* their "near-banking" competitors deserve much more acceptance in the revisions of Canada's banking legislation than they have apparently received. The greatest difficulty is that the proposed legislation does not seem to reflect realistically the developments in means of payment, in banking-type activities and in the payments mechanisms in Canada that have already taken place (and are likely to go on). This lack of realism is all the more surprising, given the brilliant observations and analysis of these issues in the Report of the Royal Commission on Banking and Finance. Some of the Commission's ideas (e.g. the extension of banking regulations to institutions not now subject to them directly) have apparently been rejected, for publicly-stated reasons that are highly questionable. Not all of the Commission's recommendations may be regarded as right, but the evolutions and the potential problems to which they are directed cannot be ignored, as the new legislation frequently seems to do.

The hard core of the Royal Commission's position is the fact that banking-type functions have been taken on to an increasing degree by institutions other than the chartered banks. Two important consequences follow from this. First financial claims other than those of the central and chartered banks, have already become a significant element in the payments mechanism, i.e., have taken on monetary characteristics that used to be confined to currency and bank deposits. Secondly, the efficiency and equity in the borrowing and lending system of the country has been influenced by these changes in institutional competition. The Commission anticipated further developments in these directions, and believed that such trends would improve the Canadian financial structure if proper conditions and regulations of all banking-type institutions were introduced.



For efficient, equitable, economically-responsive operation of the banking and monetary system in the new environment, one or other of two conditions is necessary, perhaps, as the Porter Commission suggested, both. The *first* is a close, continuous, flexible competition as borrowers and lenders between the chartered banks and their 'near-competitors'. Legislation should be directed to the vigorous promotion of such competition.

The Porter Commission's proposals for broadening the concept of banking-type institutions, for providing option to firms to enter the banking business and for limiting barriers to competition among financial institutions were important parts of their competitive route to an improved financial structure. If the competition is sufficiently close and continuous, then it may not be necessary to extend banking-type regulations to all of these institutions. Competition and self-interest may then be a sufficient regulator. A second condition, the Porter Commission thought also to be necessary; this is the extension of a minimal common set of banking-type regulations to the banking activities of all institutions engaged (in whole or in part) in a banking-type of business. The central recommendations were a set of common minimal cash reserve ratios, claims on the central bank being treated as cash throughout. Given the responsibility of the national government to create and control money; given also the responsibility of national governments for national economic well-being; given the importance of highly effective controls over monetary affairs as a means of general economic policy; then a near-overwhelming case can be made for extension of some minimum of banking-type controls to all those institutions which are engaged in a banking-type of business.

Bill C-102 does not clearly meet either of the conditions which the Porter Commission considered to be fundamental to the improvement of Canada's banking and monetary arrangements. It does not unambiguously reflect or stimulate the intensified competition of chartered banks and their near-competitors in banking activity. While some provisions of the bill appear to make a contribution toward such intensified competition for banking business, other provisions might very well turn out to be restrictive of that competition (the clearing system, for example). The old-fashioned definitions of banks are retained in all their unrealistic glory. No provision is made for the application of banking-type regulations to institutions other than the chartered banks.

Some people argue that the Porter Commission's recommendations for extending the concept and regulations of banking would interfere with provincial rights, as many of the competitors of the banks are provincially-chartered. This argument does not stand up to examination. The suggestions of the Porter Commission would give to all financial intermediaries, whether provincially or federally-chartered, the right to enter into or stay out of banking-type business; that is, the right to enter or not into the business of creating means of payment or money in the broad sense of that term. But acceptance of the option is condition on a minimal set of conditions—conditions that are considered to be necessary to the management of the money and payments system of the nation. That really matters is that the regulations of intermediaries which opt into the banking-type of business be necessary for monetary purposes; that they promote efficiency and that they be not unduly discriminatory. The privilege of opting into a new line of business, subject to a minimal set of controls that are essential

to the management of the nation's currency cannot be treated as contravention of provincial rights.

To sum up, unless controls of the clearing system and other regulations make the position untenable, it is likely that the process of diffusion of banking activities will go on in Canada. It seems undesirable to suppress such an evolution, as the administration of some features of the new Act could well do. It seems unrealistic to ignore the developments as some other features of the new Act seem to do. In my judgement redrafting of Bill C-102 and the related legislation to promote the diffusion of banking activities and to bring all banking institutions under common regulations (aimed at efficiency, equity and effective monetary management) should be undertaken.

#### *Fixed Cash Reserve Ratios and Variable Secondary Reserve Ratios*

In specifying monetary controls over the chartered banks, the new Acts are partly in accord with the recommendations of the Porter Commission. The acts do not introduce a large complicated set of qualitative instruments of monetary policy, even on a standby basis. However, the Report did not display much enthusiasm for secondary reserve ratios, which have been introduced in the Acts on a statutory variable basis.

The scheme of monetary policy implied by the new reserve arrangements should be explored. The new arrangements substitute a uniform, fixed, legally-required minimum cash reserve ratio for the potentially-variable ratio of the preceding act. They also introduce a statutory secondary reserve requirement which may be varied at the discretion of the secondary bank, to replace the agreed, fixed, non-statutory provision that has operated in recent years.

Under the previous cash and secondary reserve arrangements it appeared that:

- (1) the principal instruments of monetary controls were the open-market operations of the central bank, and the informal agreements between the central bank and the chartered banks about the operations of the latter;
- (2) the variable minimum cash reserve ratio was not intended as a normal instrument of monetary policy but rather as a standby instrument of control for use in emergencies;
- (3) the initial introduction of the agreed secondary reserve ratio system was in an attempt to influence the structure of interest rates, keeping down short-term interest rates and credit terms and pushing up longer-term interest rates and credit terms. The continued existence of the fixed agreed minimum secondary reserve ratios may have some influence, during business and credit cycles, on the timing and degree of change of certain short-term credit conditions relative to those on longer term obligations.

Is the new system intended to work fundamentally in the same way, or differently. Is the variability of the secondary reserve ratio to be a standby power for use in emergencies, or is it meant to be an ordinary continuously-used instrument of monetary policy? Or perhaps is the instrument to be used occasionally but not continuously, as the special deposit arrangements are in Great Britain or Australia? If the variations in the secondary reserve ratio are to be used as more than an emergency instrument of monetary policy, how are they

likely to be supplemented with other policies designed to influence the structure of credit conditions? Are the instruments of monetary control implicit or explicit in the Act (after the ambiguities about the secondary reserve ratio are cleared up) adequate to the job of monetary management in Canada? These questions should be answered before Parliament accepts the new legislation.

### *Conclusion*

The proposed bill C-102 should definitely be amended:

- (1) to remove the 6 per cent ceiling on interest rates on bank loans, perhaps replacing it with a set of maxima that are realistic for various classes of business and are capable of accomplishing what such ceilings may do in protecting the public;
- (2) to reduce the rigidities on bank operations in conventional mortgages, and eliminate some of the ambiguities about interest on these loans;
- (3) to shift Canada to a par-collection service, or if not to such a system, at least to a defensible maximum scale of charges for collections, not devised as a per cent of amount being cleared;
- (4) to shift the control of the clearing system to the whole of the range of institutions which play some part in the creation of instruments used in the payments mechanism, and to provide some statutory basis for ensuring efficient, equitable, non-discriminatory operation of the clearing system;
- (5) to extend the definitions and regulations of banking-type institutions along the lines recommended by the Porter Commission.

Clarification of the operation of the monetary controls should be given.

The proposed acts are by no means disgracefully bad ones; but in my judgement they could be better. Moreover it matters that they be better; the deficiencies, ambiguities and unrealities to which these comments have been pointed have considerable significance for the Canadian economy. Enormous thought and ingenuity have been devoted to drafting provisions to limit foreign ownership and control over Canadian banking. What is now required is similar thought and ingenuity to be devoted to improving the other features of the acts.



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LÉON-J. RAYMOND,  
*The Clerk of the House.*

HOUSE OF COMMONS

First Session—Twenty-seventh Parliament  
1966

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STANDING COMMITTEE

ON

**FINANCE, TRADE AND ECONOMIC AFFAIRS**

*Chairman:* Mr. HERB GRAY

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MINUTES OF PROCEEDINGS AND EVIDENCE

No. 33

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TUESDAY, DECEMBER 20, 1966

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Respecting

- Bill C-190, An Act to amend the Bank of Canada Act.  
Bill C-222, An Act respecting Banks and Banking.  
Bill C-223, An Act respecting Savings Banks in the Province of Quebec.

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WITNESSES:

- R. Caterina, Associate Professor, Accounting and Finance, Carleton University; E. P. C. Burke, General Manager, The Canadian Credit Men's Association Limited; W. E. Scott, Assistant Inspector General of Banks.

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STANDING COMMITTEE  
ON  
FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. Herb Gray

*Vice-Chairman:* Mr. Ovide Laflamme

and Messrs.

Addison,	Comtois,	Leboe
Basford,	Flemming,	Lind,
Cameron ( <i>Nanaimo-</i>	Fulton,	McLean ( <i>Charlotte</i> ),
<i>Cowichan-The Islands</i> ),	Gilbert,	Monteith,
Cashin,	Irvine,	More ( <i>Regina City</i> ),
Chrétien,	Lambert,	Munro,
Clermont,	Lamontagne	Valade,
Coates,	Latulippe	Wahn—(25).

Dorothy F. Ballantine,  
*Clerk of the Committee.*



## MINUTES OF PROCEEDINGS

TUESDAY, December 20, 1966.  
(66)

The Standing Committee on Finance, Trade and Economic Affairs met at 11.15 a.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Addison, Cameron (*Nanaimo-Cowichan-The Islands*), Clermont, Gilbert, Gray, Laflamme, Lambert, Latulippe, Leboe, Lind, More (*Regina City*)—(11).

*In attendance:* R. Caterina, Associate Professor, Accounting and Finance, Carleton University; W. E. Scott, Assistant Inspector General of Banks; Miss M. R. Prentis, research assistant.

The Committee resumed consideration of the banking legislation.

The Chairman introduced the witness and noted that Mr. Caterina had submitted a brief in 1965 relating to Bill C-102 (the Bill then revising the Bank Act) and an addendum in 1966 relating to Bill C-222; a letter from Professor J. Smyth, Professor of Commerce, University of Toronto, supporting Mr. Caterina's brief had also been circulated to members of the Committee. In accordance with resolution passed at the meeting of October 13, 1966, the brief and addendum, as well as the letter from Professor Smyth, are attached as *Appendix AA*.

Mr. Caterina summarized his brief and was questioned.

The questioning continuing, at 1.05 p.m. the Committee adjourned until 3.45 p.m. this day.

### AFTERNOON SITTING (67)

The Committee resumed at 3.55 p.m. this day, the Vice-Chairman, Mr. Laflamme, presiding.

*Members present:* Messrs. Cameron (*Nanaimo-Cowichan-The Islands*): Clermont, Comtois, Gilbert, Laflamme, Lambert, Latulippe, Leboe, Lind, More (*Regina City*), Wahn—(11).

*In attendance:* The same as at the morning sitting and in addition Messrs. E.P.C. Burke, General Manager, The Canadian Credit Men's Association Limited, and Denis Baribeau, research assistant.

Questioning of Mr. Caterina continued. Mr. Scott was also questioned.

The questioning of Mr. Caterina having been concluded, the Vice-Chairman thanked the witness who then retired.

Mr. Burke was called and, at the invitation of the Vice-Chairman, summarized the brief submitted by the Canadian Credit Men's Association Ltd. In accordance with the resolution passed at the meeting of October 13, 1966, the brief is attached as *Appendix BB*.

The witness was questioned.

The questioning having been concluded, the Vice-Chairman thanked the witness, who was permitted to retire.

At 5.35 p.m. the Committee adjourned to the call of the Chair.

Dorothy F. Ballantine,  
*Clerk of the Committee.*

## EVIDENCE

(Recorded by Electronic Apparatus)

TUESDAY, December 20, 1966.

The CHAIRMAN: Gentlemen, I will call the meeting to order. This morning our witness is Professor R. Caterina of Carleton University. He received the degree of Bachelor of Commerce from the University of Toronto; he then became qualified as a chartered accountant in the Province of Ontario and later received his Masters degree in business administration at the York University. For some years he has been associate professor of accounting and finance at Carleton University. He specialized in the fields of financial reporting, business finance and financial institutions generally, in the course of his work in the academic profession.

I would like to ask Professor Caterina to summarize his brief. Then we will proceed to the general discussion of the topics he has raised in the order he has raised them in his brief.

Professor Caterina, you may begin.

Mr. R. CATERINA (*Associate Professor of Accounting and Finance, Carleton University*): Mr. Chairman and members of the Committee, perhaps I should explain how my interest in this subject arose. I became interested at the time of the merger between the Bank of Commerce and the Imperial Bank. You may recall that at the time controversy arose as to the wisdom or otherwise of the merger. The then Minister of Finance indicated that the merger was in the public interest and, therefore, he approved of it. A colleague of mine and I got into some very hot discussions on this, his view being that banks' profits were already too high and, therefore, the merger should not have been allowed.

I tried to substantiate his claim; in other words, were banks' profits too high, and I got nowhere. One could not determine from the reports whether or not profits were high, low or indifferent. Given that, I embarked in 1962 on a detailed study of the problems of financial reporting by commercial banks. This led to two more articles and the submission in front of you.

Perhaps the problem of commercial banks financial reporting may be understood better if we first had a brief framework of financial reporting in general and then look at commercial banks reporting in this context.

First of all, gentlemen, what is the basic aim of financial reporting? That is the question we have to ask ourselves. In our society and in our economy I submit the basic aim is to inform shareholders of the financial position of the institution or the business as well as on the operating performance of that business or institution over a period of time. To be sure that the information presented by management on financial position and operating performance is fair, the law requires in the case of public companies that auditors issue a report on the fairness of the presentation, and of course fairness is measured in terms of a commonly agreed yardstick which the profession has developed.



What does financial position mean? It means essentially that on the one hand a corporation has to disclose or show all the resources or assets under management, in other words, what it has to work with. That is one side of the financial position. The other side will disclose the way in which those resources were financed or acquired. Therefore we have here the resources on the one hand and on the other hand, the management's modes of financing such resources. As we know there are two basic methods of financing assets, debt and equity. The creditors of a company do have fixed dollar claims. The owners have only a residual interest with no fixed claim.

The second statement of operations, which we may also call income statements or profit and loss statements, aims at portraying the results of the previous year's operations. I submit the essential purpose of this statement is to indicate the efficiency of the company's management which results in profits or losses.

This is the basic framework of financial reporting as we know it now. What has been the trend in it? In other words, has there been more information supplied to shareholders, or less, over the years? Evidence indicates that the quality of the information has improved and the amount of information disclosed by corporations has been increasing, and so has the frequency with which it has been made available. What accounts for this increasing amount of information being made available? What spurred it? I submit there were perhaps a number of factors: changing management attitude; increasing financial literacy on the part of the public as a whole; the law's increasing legal requirements; the demands of financial analysts and last but not least, the ethics of the accounting profession to see to it that adequate information be presented. Gentlemen, there could be other factors but these are some, shall I say, that have led to an increasing release of information. Incidentally, banks too have played quite a role in this by insisting that the borrowers prepare and present to them more and more information. In this way, one might say that bankers have had a substantial effect on improving reporting by industrial and commercial corporations.

In this framework let us now look at commercial banks' financial reporting. We have seen that the basic tools of financial reporting are the statement of financial condition, the statement of operation, and then the auditor's report on both of them. If we confine ourselves to these three instruments alone and try to compare bank's reporting with that of industrial and commercial corporation as a whole, the only conclusion I can draw is that banks have not kept up with the times. To be sure, banks have strictly adhered to the letter of the law. They have not violated it. Every word of the law has been adhered to. Aside from that they have not done anything else. In a real sense, as things now stand, it is impossible to make much sense out of commercial bank financial statements. Is there a reason for this? I submit there is. The situation is not peculiar to Canada. It also prevails to a further degree in the United Kingdom, because whereas Canadian banks go as far as disclosing the amount of tax expense for the period, banks in the United Kingdom do not. The reason for it, in the words of the chairman of the London Bankers Association, is that disclosure of the tax expense might in fact lead to disclosure of more information than a bank ought to disclose.

On the other hand, the situation in the United States has changed drastically in the past five years. Until then it was not much different from ours, but in the

past five years they have been going ahead at a very quick pace. Why have American banks taken the lead in improving their financial reporting? One reason, gentlemen, is that shares of American banks were not approved for listing on the New York stock exchange because, even though they provided the same information as Canadian banks do, the exchange's requirements were such that banks could not meet them, and therefore, their shares were not listed. One could buy shares of American banks on the curb but not on the big board.

The question which comes to my mind, gentlemen, is this. Is there a justification for banks to still carry on in this fashion? Is there a reason for us having, say, two sets of laws or two sets of standards, one for industrial and commercial corporations and one for banks? I do not think so. In my judgment commercial banks ought, in their own interest and that of shareholders and the community as a whole, prepare, present or provide adequate information on financial condition and operating performance.

The CHAIRMAN: Thank you professor Caterina for this very useful preliminary submission which, I think, is a framework for discussion of your brief specifically.

Professor, before beginning the questioning, will you agree with me when I say that your brief is really in two parts, your original brief on Bill C-102 and then an addendum reflecting the changes in the new bill.

Mr. CATERINA: Yes.

The CHAIRMAN: Then there is something you did not know about, a testimonial from one of your professional colleagues, Professor Smythe of the University of Toronto. He has written us, and apparently supports your views, although interestingly enough you were not aware of this until I showed it to you before the meeting began. I do not know whether this is the type of advertising that the prices inquiry would be in favour of or opposed to, but I presume that under the circumstances they would support this as well because of the source.

Our practice has been to deal with these matters in the order of the topics raised. Perhaps I should ask you this question. To what extent would you say that you have taken into account in your supplementary brief not only the changes in the new bill but the amendments which were tabled at the beginning of our hearings for our preliminary considerations?

Mr. CATERINA: The amendments, or at least some of them, of October 25, 1966 take care of three points raised in my additional submission.

The CHAIRMAN: Perhaps you then could take another few moments, so that we will not take time inadvertently discussing them, and just deal with how these amendments were taken into account in the points raised. Would this meet with the satisfaction of the committee?

Some Hon. MEMBERS: Yes.

The CHAIRMAN: I am referring to your submission of October 31.

Mr. CATERINA: Yes. You may recall that the bill introducing schedule P and clause 63, dealing with the auditor's report, does not include reference by the auditors on schedule P.

In my judgment that schedule is as significant as the other two and therefore the auditors ought to report on it as well. This amendment, in fact, provides for it.

The CHAIRMAN: You are referring to the amendment to clause 63.

Mr. CATERINA: Yes.

The CHAIRMAN: And this deals with the points that you have raised on page 3 of your supplementary brief, where you make a criticism of the requirement of the auditor's report on only two of the schedules referred to, and one of the amendments tabled at the beginning of our hearings in effect meets that objection.

Mr. CATERINA: Yes. Another point which I might raise as well, sir, is that Schedule P left out general reserves. In other words, schedule P, as initially stated or presented, had an item called "Transferred to tax-paid association", and nowhere in the schedules is the amount of the balance of this item shown. Therefore, I requested that whatever the amount is, this be disclosed and that the same information be shown for it as it is for the other types of reserves. The amendment does take care of that.

The CHAIRMAN: This point, in effect, has been recognized in the amendment.

Mr. CATERINA: Yes.

The CHAIRMAN: Did you say you had three points to make?

Mr. CATERINA: There were two points.

The CHAIRMAN: And these have been met by the amendments tabled October 25th.

You have said in the introduction to your addendum that you wished to draw the Committee's attention to the points raised in your original submission which are equally applicable to Bill No. C-222. What do you infer in that regard with respect to the points in your original brief to which you do not make reference in your submission?

Mr. CATERINA: Briefly, what I mean to say is that whatever I have said on Bill No. C-102 is equally applicable to Bill No. C-222.

The CHAIRMAN: But you wished to draw special attention—

Mr. CATERINA: To certain items in this brief.

The CHAIRMAN:—to certain items in this brief. If that is the case—and I was going to suggest this anyway—you have an introductory section which in effect fits into your introductory remarks in the original brief. You have: introduction, the present state of chartered banks reporting to the shareholders; the views of the royal commission on banking and finance, Bill No. C-102: its provisions, on annual statements and shareholders' audit. I might characterize this as the general background of your submission. I would suggest to the Committee that we begin our discussions on these general topics which would fit into your initial presentation that I have just mentioned, and then move along to the topics in your original brief and deal with any in the addendum that have not been covered. Does this seem like an orderly way to do this? Some of the topics are rather technical and I suspect that we may not want to attempt to engage in an



accountant's equivalent of a discussion between lawyers on legal matters on which Mr. Lambert has cautioned us about on several occasions.

I would invite the Committee to begin questioning on the general background remarks made by Professor Caterina which, in a sense, arise out of the topics I have referred to in the first four or five sections of his initial brief. I will recognize Mr. Clermont.

*(Translation)*

Mr. CLERMONT: Mr. Chairman, if I have understood your remarks correctly and the remarks of the professor, he has made himself aware of the suggested amendments.

The CHAIRMAN: Would you repeat your question, please, Mr. Clermont?

Mr. CLERMONT: In your remarks following the summing up given by the professor, you have put a few questions with regard to the amendments suggested by the Inspector-general and tabled by him. According to the witness do the amendments suggested to 60 to 63 meet with the objections he has made in his brief with regard to C-102 and C-222?

*(English)*

Mr. CATERINA: Yes, the amendments do meet my recommendations on pages 1 and 2 of my addendum. Because no indication of reserves for contingencies is provided for by Schedule P, the initial recommendation that I make in the addendum is that it should be amended so that this information may be available. The amendment to clause 60 (2) (c) reads:

A statement of the accumulated appropriations for losses of the bank for the financial year, showing the information in the form specified in Schedule P and such additional information and particulars as in the opinion of the directors are necessary to present fairly the amount of the provision of interest to meet losses other than those for which specific provisions have been made.

So this amendment takes care of one of the points I raised in the addendum.

*(Translation)*

Mr. CLERMONT: With regard to the accumulated reserves or reserves on which taxes have been paid and which it is possible for the banks to deduct from their annual profits and which are entered into another type of reserves, are you satisfied with annex or appendix "P" as amended, or the amendments in annex "P"?

*(English)*

Mr. CATERINA: We are jumping around a bit. I was hoping to take things one at a time but if you want to deal with this now I shall do so.

The CHAIRMAN: This may be impractical because of the very detailed nature of the brief, but I thought that we might deal with the specific points raised by Professor Caterina roughly in the order he has raised them in his brief and that we might now discuss in a general way the philosophy behind his recommendations, the philosophy of bank reporting and so on which he presented to us in his initial remarks. It might be easier for Professor Caterina to comment on your

questions and those of the other members if we deal with the specific items in the Schedule roughly in the order he has presented them in his brief.

*(Translation)*

Mr. CLERMONT: Mr. Chairman, the professor's brief deals especially with 60, 61, 62, and 63; in these clauses there is mention made of the reserves—general or special reserves, so called.

At any event, this is my question. I am not sure whether I am in order or not, but in the brief relating to bill C-102, i.e. in sections 5 and 6, it is stated that in the reports made by the banks to shareholders, there should be a distinction drawn between general and special loans. Could he tell us why this preference?

*(English)*

Mr. CATERINA: If I understood correctly, the question asked is a distinction is wanted between business and personal loans.

Again, this is jumping a step ahead but let us deal with it now. In my judgment, the two types of loans do involve different types of risk. In other words, there are two different types of assets. Their quality is different. And if this is the case, as I think it is, why combine two assets with different characteristics under one heading? Why not follow the same procedure as for deposits where personal savings deposits are shown separate from other deposits? If the distinction is valid for the deposit side I submit that it is equally valid on the asset side of loans.

*(Translation)*

Mr. CLERMONT: In your brief, with regard to Bill C-222, you object to the banks indicating in the assets and liabilities the securities, letters of credit and so on.

*(English)*

Mr. CATERINA: On this point, sir, perhaps I have to give some background here, as the brief does. A guarantee or letter of credit is not a prime liability of the bank in the sense that the bank will become liable only if and when the prime debtors fail to meet their obligations. I suppose it is safe to assume that before a bank dares grant its privilege of a guarantee or letter of credit the bank makes very sure that the funds will be made available to it by the customer ahead of time, or at least at the maturity date of the obligation. This being the case I submit that these are fictitious liabilities and have no place in financial statements. The same argument applies to the asset side of it. There we find an item of equal amount; the contra shows an asset. If we understand an asset as something of economic value to which the corporation has a right it is obvious that these contingent liabilities give rise to contingent assets and there is no place in any set of financial statements for contingent assets. Therefore, in my judgment the only purpose that these two items serve in the statement is to inflate the total, and nothing else.

The information relating to this contingency may well be disclosed by way of a footnote as is done with commercial and industrial corporations which may have some contingency. In fact, as I indicated in my brief, in 1964 the Morgan Guarantee Trust Company did follow the practice of excluding from the assets and liabilities the guarantees and so forth, and showed them as a footnote to financial statements.

(Translation)

Mr. CLERMONT: Thank you, Mr. Chairman.

The CHAIRMAN: Thank you, Mr. Clermont.

(English)

I suggest that it may be slightly unrealistic to expect a completely separate area of discussion on some of the points of Professor Caterina's brief which may be very specialized. I am wondering if we might not try a slight departure from our practice and that questions be based on the general matrix or background of his brief, which is reflected in pages 1 to 4 of the initial brief in addition to his introductory remarks, in the course of which some reference may be made to specific items, but with the exception, I think, of inner reserves which is a very important topic and stands entirely by itself—also with the exception of his comments on auditors' reports to shareholders, which he has also singled out in his addendum. Perhaps this might make it a bit easier for members who may feel that it would be unduly technical to try to deal otherwise with some of the other specific points. I do not think we should depart completely from our very successful procedure of dealing with the topics raised by our witnesses in the order they raise them, where that can be done, but we might attempt this because of the somewhat different nature of Professor Caterina's brief. In that spirit I recognize Mr. Lambert.

Mr. LAMBERT: First of all, Mr. Chairman, I find myself in fundamental agreement with the general philosophy of Professor Caterina's brief although, perhaps, I would not go as far as he does on particular items.

Do you not think that one of the distinguishing features has been that in the past the distinction between the banks and an industrial or manufacturing concern has been that the banks have not had to resort, shall we say, to the public market for additional shares either of a common or a preferred nature and, therefore, they are not trying to interest an investing public; but now that there is a provision for the banks selling debentures to raise long-term funds, within a year a good deal of what you are asking for will be forced upon the banks by what you might call a more financially literate investing public? If they are coming to the market to sell debentures, people are going to say, "Am I going to buy or am I not going to buy?" At the present time there has not been that case. It is just a case of: "Do you want bank stocks as an investment? Their dividend records are there". This is the criterion. They have been the bluest of blue chip stocks, and it is a dividend record. The general public does not require that information. Now that they are coming into debentures I think that you may see this as a natural evolution. Having said that, do you not think also the distinction in the operations between the banks and any other commercial institution is the fact that banks do not provide really meaningful statements for the investor. I maintain that the type of statement that is really the crucial one is not the balance sheet for an industrial concern. The one I would want to look at is what has been known as "The Source and Application of Funds". Which shows where the money came from and what they did with it. That is the measure of efficiency.

But you cannot do that in a bank. Where does the money come from? What do they do with it? Because it would be completely distorted and it is for that reason that it is very difficult to get an equivalent of source and application of



funds. Really this is what you are getting at in your brief. You would like to see a sort of source and application of funds.

Mr. CATERINA: Not exactly, sir, for two reasons, really. I submit that a statement of source and application of funds is not one which points up efficiency but rather it merely explains one aspect of over-all company operations. That aspect is the financial management of the corporation. The corporation did get a certain amount of funds from various sources. How were these used? So, in the real sense, I must admit that statement is one that explains the activities of the treasurer if that can be said.

Mr. LAMBERT: It is from a shareholder's point of view that this is really meaningful.

Mr. CATERINA: Yes, it is. I would not deny it. All I am suggesting is that it is not a statement whose purpose it is to point out the efficiency or otherwise. It merely explains the company's financial policy.

Mr. LAMBERT: Well, we have different views on the efficiency of that type of statement or the value of that type of statement. To what degree do you feel, though, that a corporation, such as a chartered bank, should disclose information to the other bankers and its competitors which will really open its books to its competitors. Now, there is always this, and I think a very legitimate point too—

Mr. CATERINA: I might answer your question, sir, by looking at a non-banking institution or, shall we say, industrial and commercial corporations; let us put it that way. Now, to what extent are these to disclose information? We have two examples, three companies, if you like and some of you may be perhaps conscious of this now: Steinbergs, Dominion Stores and Loblaw's. They are three companies essentially the same at least on the surface. They are in the same type of business. Now, if you look at the financial reports of these three companies you will find that the one disclosing the most is Dominion Stores; the one disclosing the least has been Loblaw's and the one in between is Steinbergs. Either the Dominion Stores, shall we say, has closed down markets or lost business because it chose to be a step ahead of legal requirements. In fact, the contrary is true. If population has any value I would suggest that Weston's practice has been inimical to it vis-a-vis Dominion Stores, which has won annual prizes for its report for the last 10 years or so. So, the question, I think, boils down to this. If management—and I speak in very broad terms now, sir,—is entrusted with the management of their pile of resources should it not be made accountable for the way it uses them, for the results it gets from them. This, of course, is a philosophical issue and, perhaps, I may even state it more forcefully this way. Is confidence, as expressed in commercial banks, maintained through ignorance of the facts or through knowledge of the facts? Is confidence maintained when an institution is able to hide a loss somewhere, so people will not know? Or, is it maintained when the facts are known and people can judge for themselves?

Mr. LAMBERT: Well, to take up your argument, I would think that you certainly are putting forward a case that in their own interest they should disclose more. But, all the average public company is required to do is file a balance sheet, file a profit and loss statement with the registrar of companies for public examination. This is in connection with public companies.

Mr. CATERINA: Private companies, sir.

Mr. LAMBERT: All that private companies have to do is file a statement. There is a distinction between what is required of a public company by, I suppose, stock exchange regulations and other legal minima. In so far as the private companies are concerned, they have frankly no legal minima except that they must file a statement. It does not say all that it has to have.

The CHAIRMAN: Are we comparing banks with private companies or with other companies?

Mr. LAMBERT: It is a fundamental portion of Professor Caterina's brief. Some of his comments go not only to the nature of bank financial statements but the whole of corporate financial reporting. It applies not only to banks. He feels that there should be much more than is now disclosed. Am I not correct?

Mr. CATERINA: Perhaps not to the extent that you might want to imply, sir. Let us put it this way. My philosophy is a very simple one. I tried to reconcile myself between the ideally attainable; that is my basic philosophy. In so far as non-bank corporations are concerned they are doing a fairly good job I should say but they could improve. The problem with them, as I see it, is not as important with them as with the banks.

Mr. LAMBERT: Mr. Chairman, I will finish that series of questions and then go on to particular items.

Mr. CHAIRMAN: By the way, as far as organizing our discussion is concerned, what I was really driving at was this. If you look at Professor Caterina's brief and its addendum, you will see there is a general discussion on pages 1 to 4, then there is a discussion of the items on the asset side of the balance sheet and then a discussion of the items on the liability side of the balance sheet. Perhaps I did not express this as clearly as I had it in mind but what I would suggest to the Committee is that first we have our questions on the general discussion raised by Professor Caterina and then we could discuss the items on the asset side—which is the way he set it up in his brief—then the items on the liability side with the setting aside of the question of inner reserves as a special topic on the liability side. Maybe we could discuss the asset side all at once because the items are perhaps of a more technical nature. This was what I was driving at. Perhaps I should apologize to the Committee for not explaining what I had in mind as clearly as I had intended to. I now recognize Mr. Lind. We are continuing our questions on the general matrix of Professor Caterina's submission.

Mr. LIND: Professor Caterina, with regard to the banks, it was pointed out to us that the banks are becoming more and more departmentalized. They have the department for consumer loans; they have commercial loans, they have loans to their purchase of security. When we come down to the statement of their assets and liabilities, is it your contention that this should be departmentalized, too, so that we can see in which category they are making a fair gain or they have losses?

Mr. CATERINA: Yes and no, sir. My recommendation for segregation of loans by major components, as I suggested a while ago, is based on a different premise. They are all loans, yes, but I submit that a commercial loan is of a different nature from a personal loan. I presume that banks do carry out different types of analysis in granting either type of loan because the risk is different. Now, to

the extent that the two assets, shall we say in the case of commercial loans and personal loans to sort of limit the category, do entail different risks, then, perhaps, a case could be made for indicating the proportion of the total loans which are personal and those which are business loans. It is the same, you might say as you look at—now again if I might go to the industrial and commercial field—there we have different types of assets, inventories for instance. There are inventories all right, but when the components of it are of a significant amount, then this corporation does show them separately. A case in point, perhaps is Massey-Ferguson for instance, a manufacturing enterprise; it has inventory in working process and finished goods and raw materials. They are assets, yes, but of different types.

Mr. LIND: Now with regard to the write-offs by banks to the various categories, is it your opinion that these write-offs against their special reserves and contingency reserves, should be made public?

The CHAIRMAN: Mr. Lind, your question is quite in order but I thought we had agreed, at least informally, that we reserve our questions on that area of Professor Caterina's brief until we come to it later on. It is specified later on under the heading of Bank Liabilities. This may permit a more orderly discussion, if we try and stick to that approach. The question, generally, is quite in order, but I thought we had agreed to attempt to first deal with the general philosophy, if I may put it that way, underlying Professor Caterina's submission, then the items he has listed under the heading Assets, then the items he has listed under the heading Liabilities. And under liabilities there is a specific item entitled "Reserves". This is a very important topic. I think the Committee may want to deal with it separately.

Mr. LIND: Well, all right, Mr. Chairman, then I would like to ask Professor Caterina another question. You mentioned that the American banks could not have their shares listed on the exchange owing to the fact that they did not adhere to complete disclosure of the exchange. How does this apply to our Canadian banks?

Mr. CATERINA: Our banks are listed.

Mr. LIND: Yes, I know.

Mr. CATERINA: But perhaps, shall we say, we are somewhat more trusting.

The CHAIRMAN: Are our disclosure standards of our securities exchanges as high as the American?

Mr. CATERINA: I submit not.

Mr. LIND: I will pass, Mr. Chairman.

The CHAIRMAN: I will recognize Mr. Gilbert.

Mr. GILBERT: Mr. Chairman, Professor Caterina has set forth his reasons for the necessity of disclosure: firstly, to set forth the financial position of the bank and secondly, so shareholders can watch the performance, or, I should say, analyze the performance of the management. I think that is your basic philosophy. Then you have come forth with suggested amendments. In your appendix you have set forth a model of a United States bank, the First National Bank of Chicago. What I would like to know is, do you feel (a) that schedules N, O and P are not sufficient, and that this model is sufficient? If that is your position, maybe



we should study the items where you have suggested that changes be made. Then you could compare your suggested changes with the model that you have at the back because your model is really an expansion of disclosure. You must be saying that N, O and P do not disclose the information that shareholders should be entitled to as set forth in the model. Is that your position?

Mr. CATERINA: Perhaps you will let me make a comment or two on that. The example is not the ideal. It is a better one than the one we now have in Canada.

Mr. GILBERT: In other words, we should be moving towards this type of disclosure.

Mr. CATERINA: Yes, very much so.

Mr. GILBERT: That is why I think it would be wise, Mr. Chairman, if we moved into these specific items and then at the end Mr. Caterina can compare the model with what we have at present.

Mr. CATERINA: It is not a model, it is an example.

Mr. GILBERT: All right, an example.

Mr. CATERINA: It is not the ideal. A better one can be found this year if one looks, for instance, at the First Wisconsin Bank Share Corporation. They are far ahead of what I have here.

The CHAIRMAN: Perhaps we could ask one of our researchers to find the report for us on the Wisconsin Bank which we may look at later on.

Mr. CATERINA: That is the Wisconsin Bank Share Corporation.

The CHAIRMAN: In that light, are there any questions of a general nature which we want to deal with now before proceeding to the items? Mr. Cameron?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Professor Caterina, I noticed that your brief lays great emphasis on the need of providing this information for the benefit of shareholders. Frankly, I have never lost very much sleep about the welfare of bank shareholders and I am just wondering whether you also consider that this revealing of the financial operations of the banks has perhaps a wider application in that the general public should be informed of how these crucial institutions to whom parliament has given a legislative framework are carrying out the functions that have been entrusted to them. To me this would be a much more compelling argument for this sort of thing than merely the protection of the shareholders. I am wondering if you had the general public in mind but had not put it in this context.

Mr. CATERINA: Sir, to be very frank with you, my initial thought, was the public interest, but how does one measure it? So I shifted and focused my attention on a specific group which I identify very clearly.

The CHAIRMAN: Yes, totalling some 100,000.

Mr. CATERINA: Yes. So, sir, it is not disregard for the public, no. The problem was I could not deal with them but with a specific group I can.

Mr. LAMBERT: Is not the public interest served by the statutory requirements filed with the Inspector General of Banks? Is not that where the public interest must be served?

Mr. CATERINA: The question then, to my mind, would be this. Do we, as individuals, have any right to decide such a thing for ourselves or must we let the government take care of our needs. I am a strong believer in our economic system as it is. I want to preserve it that way.

Mr. LAMBERT: Well, I think that introduces a slight misconception. I agree with the public knowledge from the point of view of the shareholder which is primarily what you are after but the real public interest is in the safety and the, well, honest management of the bank and that is gathered in through your reports to the Inspector General.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): With all due deference to Mr. Lambert, Mr. Chairman, I take it he has completely misinterpreted my idea of the public interest. I do not think at this particular juncture in our financial history the public has any doubts about the financial safety of the banks; but there may very well be some doubts whether these institutions are functioning as efficiently as they should in the general economic context of our society. In fact there may very well be, and I would like to ask you to consider this Professor Caterina, as a result of these further revelations, indications that there has been a conflict between the interests of the group on whose behalf you ostensibly have brought your brief, and the general public; that the maximizing of profits for instance, may have taken precedence over a more efficient operation of these institutions for the general conduct of our economy. I wonder how you solve the possibility of that conflict, by concentrating on the shareholders.

Mr. CATERINA: Well, sir, your question could be answered if it were possible to set up two models, shall we say. In other words, forget the reward, or look at it and assume on the possibilities of what the result might have been if a course of action were taken as opposed to another. Now, I do not know how this can be done sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No. Thank you.

The CHAIRMAN: Well, I think we should note the very interesting development here, when we find Mr. Cameron and Professor Caterina on one side of this particular question, and Mr. Lambert on the other.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I would be very happy to have Professor Caterina on my side.

Mr. CATERINA: Gentlemen, I am really for each side.

The CHAIRMAN: You should be in politics. Mr. Laflamme—Oh I am sorry, are you finished Mr. Cameron? Mr. Laflamme.

Mr. LAFLAMME: Mr. Caterina, in the last paragraph of your brief you say that "if in the past limited disclosure was desirable to maintain public confidence". Do you believe that?

Mr. CATERINA: No.

Mr. LAFLAMME: So this is only a hypothetical question.

Mr. CATERINA: Well, I suggest if it were—

The CHAIRMAN: In fairness to Professor Caterina, I do not think he advanced this as an argument, he said in effect, for the sake of discussion if this was the reason before—

Mr. LAFLAMME: But I am sticking to that point.

The CHAIRMAN: Yes, page 18.

Mr. LAFLAMME: Do you precisely think that the question of taking the shareholders into the confidence of the bank is the main reason why the bank did not disclose all the assets and liabilities?

Mr. CATERINA: Well, perhaps sir. If we look at the philosophy, you might say, or if there is one philosophy, I am afraid that bankers, and perhaps quite a few of our business as well, have always had in front of their minds, a return of the depression, collapses, catastrophes, and all that which would result from such situations. And to sort of avoid the likelihood or the possibility of people panicking, shall we say, they chose not to make them fully aware of the facts. It is a sort of what I call depression psychosis; that is the only way I can put it.

Mr. LAFLAMME: You believe, or you think, that banks do not disclose their assets because it would not be good for them to show that they were not as rich as the people felt they were.

Mr. CATERINA: I do not know what their views or reasons were frankly, because I cannot think for them, I cannot guess for them. I know the facts, I have a statement. Now why they chose not to, perhaps the latest figures I have of that is again one given to the Jenkins committee in 1960 in the United Kingdom and Sir Lloyd Franks who was simultaneously chairman of the London Bankers association, and chairman of Lloyds Bank. In this testimony he made a real case against disclosing reserves and operations primarily because the public does not understand them, No. 1. No. 2, it would be dangerous if this were made known. Also, shortly prior to it, the United Kingdom banks had suffered substantial losses, and he claimed that they were able to cover them up—that is my expression, O.K.—by drawing on the inner reserves for one year. In so doing, no one really knew what happened, and the calmness was maintained. Now, is this sound advice? I think not; that is my view of this question, I think not.

Mr. LAFLAMME: But do you not think that some other purposes could have been served by the banks in making up their balance sheets as they usually did?

Mr. CATERINA: I do not know, sir; I honestly do not know.

The CHAIRMAN: What you are driving at is perhaps there were other conventions or principles of accounting in those days.

Mr. CATERINA: Well, yes. Well, let us look at it this way. The accounting has changed dramatically in the past 20 years, especially in the last 10. These changes have been reflected, in candour, in the United States as well, in changes in legislation, so that as accounting standards, you might say, change, then these changes were brought into the various sanctions. In addition, we have heard that the accounting profession both in the United States and Canada, has been quite helpless in pushing for various codes of information, and it has been achieved. Now, somehow it would appear that the chartered accountant in the profession, and the sanctions, shall we say—call them bank sanctions—have been able to attain better results in the non-banking field than with the banks. We have had quite a few cases of industrial and commercial corporations, which in a real sense have gone far ahead of the minimum vis-à-vis requirements, quite a few of them.



The CHAIRMAN: You are referring particularly to publicly held corporations?

Mr. CATERINA: Yes, publicly held. That is what he wants to know so when I say that I refer to the company, instead of the public.

Mr. LAFLAMME: This is my final question Mr. Chairman. On page 3 of your brief you quote the Porter Report as follows:

In our view, the goal of protecting the public against loss can be best achieved with three basic legislative safeguards—adequate disclosure, competent supervision and legal powers giving the authorities the right to force the correction of unsound or careless practices and to prosecute those engaged in fraudulent or criminal activities.

Do you think that the Porter Commission at the time was referring to the activities of the banks or to the activities of other financial institutions?

Mr. CATERINA: It says the commission was on banking. I assume that he was referring to banks specifically.

Mr. LAFLAMME: Thank you, Mr. Caterina.

The CHAIRMAN: Mr. Addison.

Mr. ADDISON: I would like to ask Professor Caterina this question: In your studies did you notice any difference in the method of behaviour of a minister of finance in dealing with facts, let us say, the hon. Donald Fleming, or Walter Gordon or Mitchell Sharp. After all the Inspector General of Banks is reporting to these gentlemen. Have you noticed any difference in the way that ministers of finance would look at banking?

Mr. CATERINA: In which respect? My concern sir, is confined to the financial reports.

Mr. ADDISON: Well, you are suggesting that we have fuller disclosure.

Mr. CATERINA: Yes.

Mr. ADDISON: You are suggesting, I assume, that the banks should have tighter surveillance perhaps by the public rather than by the government. That is what you were saying to Mr. Lambert, I believe. But I was wondering, other than a basic philosophy, is there any difference between the different ministers of finance in looking at banking in Canada, in so far as the report to the Inspector General of Banks is concerned?

Mr. CATERINA: Now, confirming my remarks to my topics, I must say that over the past 30 years, we have had quite a number of ministers of finance and yet the annual reports have been identical.

Mr. ADDISON: They have been identical?

Mr. CATERINA: Yes, the facts have not changed, and the banks have gone by the letter of the law.

Mr. ADDISON: I understand that the Minister of Finance has the final authority to say what is going to be a rest account; in other words, what tax is going to be paid.

Mr. CATERINA: But that is a different issue from the disclosure that we are dealing with, because the Minister of Finance has the ultimate say on the

maximum amount banks ought to be allowed as tax free appropriations, but no Minister of Finance or because the Bank Act has not changed, has ever made attempts at asking banks to disclose the appropriation. To answer your question more directly, since actions of the past three decades have not changed, and the ministers of finance have, then I suppose there has been no change, except in the head of the department.

Mr. ADDISON: I have one last question. Do you feel that a staff of three on the Inspector General of Banks' staff is adequate?

Mr. CATERINA: I do not know, sir.

Mr. ADDISON: Thank you.

The CHAIRMAN: Mr. Leboe.

Mr. LEBOE: I was interested in Mr. Caterina's statement that there was much more disclosure in the United States than in Canada. I wonder if he could give us some background on why he thinks this particular situation has arisen in the United States?

Mr. CATERINA: Perhaps one very important explanation can be found in the S.E.C.

The CHAIRMAN: The Securities Exchange Commission.

Mr. CATERINA: That legal government organization has done more to improve on corporate reporting than perhaps all other organizations put together.

Mr. LEBOE: Would you say that generally speaking in the United States and in Canada, there has been more emphasis in the halls of learning on corporations, corporate structures, financing, and including banking, in the last five years, than there has been previously?

Mr. CATERINA: I missed the first part of the question; could you repeat it?

Mr. LEBOE: I was wondering whether the higher education facilities that we have, engaged in a clearer curriculum—if I could put it that way—in connection with corporations, corporate structures and particularly banking within the last five years. Has there been more information given to university students and the people who are studying this than there has been in the past?

Mr. CATERINA: I must speak for myself, because I have touched on that. I have been teaching this one course for the past five years, and during the period of the Porter Commission this report was discussed with them, and when the report finally came out, it was discussed. We had a seminar and it was discussed at this time. In my accounting classes when dealing with reserves specifically, I never missed the opportunity to indicate how poor this situation was in so far as the banks are concerned. To answer more specifically, in Canada we have courses in money and banking; we study the economics of money and banks, but we do not have universities offering courses dealing with the operations of banks.

Mr. LEBOE: Specifically, this is the area I was interested in.

Mr. CATERINA: I do not believe we do. The operations are treated from an economic aspect. This was the course I took.

Mr. LEBOE: If you are of the opinion that the banks should make fuller disclosures in order to get a clearer picture of the banking operations—which I

understand you are asking for—would it not be reasonable to expect that even in high schools we should be getting a much clearer picture of the full operation of our banking institutions than we do at the present time?

Mr. CATERINA: Well—

Mr. LEOE: To enlighten the public on just exactly what is taking place in our financial institutions?

Mr. CATERINA: I would assume that this would be taken into consideration. In the high schools they offer courses in business or broad economics, you might say. There again, what is covered in institutions from an economic point of view and what we are discussing here today is too technical and too deep. I am trying not to make it that way, but it is too technical and too dry to attract the imagination of the youngsters, 15 or 16 years old.

Mr. LEOE: I have found in discussing banking and financing to a degree—and I am not very expert in it—with youngsters at the age of 15, 16, or 17 that they are keenly interested in some of these things, and yet the courses of study that we have in the country today, even in universities, do not come into the financial aspect nearly as much as the economic aspect.

Mr. CATERINA: I would have to agree with you.

The CHAIRMAN: Mr. More, you are next.

Mr. MORE (*Regina City*): On page 18, in your final paragraph, you say:

If, in the past, limited disclosure was desirable to maintain public confidence, it can only be said that today, inadequate disclosure can only serve to dispel public confidence. . .

What evidence do you have on which you base this pretty definite statement? Do you think that the people who keep their money in a sock, and did under present regulations, would bring it out and put it in the banks if more information were disclosed to the public?

Mr. CATERINA: I am not suggesting that. What I am suggesting is this. Today's population is not what it was 30 years ago.

In other words, we assume that we are somewhat more sophisticated and knowledgeable now than 30 or 40 years ago; we want to know what is going to happen. Now, if this assumption be true, then, in my judgment, the less the amount of information conveyed to the public, the less satisfied the public will be. Again, this is not a fact, but a point of view based on what we think we are, and how we think now, and how they thought 30 years ago; this is it.

Mr. MORE (*Regina City*): Well, what is the reflection today on past performance and the past methods of disclosure, or limited disclosure, or inadequate disclosure? Is there any real evidence that this has brought the public to distrust and have a lack of faith, as you state?

Mr. CATERINA: No, but it has done this, though, it has sent the financial analysts and me on the road. I am today's generation, just as you are, and even with the standards that prevail today in our society I cannot accept, in honesty, what the banks are disclosing. Now, we have *Financial Post* writers expounding the same view; also the *Financial Times* of Montreal and the *Globe and Mail*, so there is at least, shall we say, amongst those who write—let us put it that



way—a discontent. I would assume, as more people read those people who write, this discontent is bound to transmit itself and reach, as we would say, the grass roots. This is not to be taken that people will take only account of the banks; I am not saying that.

Mr. MORE (*Regina City*): Do you have any evidence that this has reached to the shareholders in these banks?

Mr. CATERINA: I do not have any; I do not know.

Mr. MORE (*Regina City*): Discontent?

Mr. CATERINA: I do not know that so I will not comment on it.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Chairman, may I ask a supplementary question?

The CHAIRMAN: Yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It occurred to me when I read this last paragraph, in Mr. Caterina's brief, that this has reference perhaps to his first idea which he said he had been obliged to discard. The public confidence, which you fear is being dispelled, is not public confidence in the stability of the banks, but in the discharge of their functions and their use of the tools that have been placed in their hands for the development of our economy. Would that be the public confidence you feel is declining? I do not think you can mean that the general public feels the banks are going to collapse?

Mr. CATERINA: Oh, no.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The lack of public confidence is whether they are doing an effective job.

Mr. CATERINA: I wonder, and as long as I do, then my confidence is not 100 per cent, is it?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No.

Mr. CATERINA: Unless some question marks are erased.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But your confidence is not at all diminished in their stability.

Mr. CATERINA: Oh, no, far from that.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It is whether they are doing a good job or not.

Mr. CATERINA: In other words, are banks special institutions to be accorded special treatment? That I challenge.

The CHAIRMAN: What you are saying, in effect, is that today there is no reason why banks should not meet the same levels of disclosure as publicly held non-financial institutions.

Mr. CATERINA: Exactly.

The CHAIRMAN: And that without this information, the public at large is not in a position to assess fully and properly the performance of the banks as parts of our economy.

Mr. CATERINA: Yes.

Mr. LEBOE: Mr. Chairman, I think many people are of the opinion—rightly or wrongly—and I think this is the only question, that they are not certain that the banks are paying their fair share of taxes. Now, I am not going to ask him to comment on that; but this is a view that is widely held. Without naming anybody, or anything, I think that what Mr. Caterina has said in regard to disclosure would dispel this idea, and it is quite broadly held in the country.

Mr. CATERINA: Again, if I may express my own view, I do not care what they do as long as they are stable. I do not want to impose any limitations, or ceilings, or restrictions; do as you think fit as a manager but sometimes account for it.

The CHAIRMAN: I was interested in a comment you made in your initial presentation, that banks, in a sense, have helped this higher standard of disclosure on the part of public corporations by insisting that borrowers present them with more information today than was necessary in the past. You are suggesting, in other words, that the banks are insisting on higher standards from others than they have been willing to live up to themselves in the past.

Mr. CATERINA: Oh, very much so. In fact, any business, or individual applying for a loan today will have to provide much more information to the bank than was the case in the past.

The CHAIRMAN: If a bank had to get a loan from another bank, and provided only the information it has to provide by statute today, do you think it would get the loan?

Mr. CATERINA: No.

Mr. LIND: Regarding the amalgamation of the four banks that took place lately, namely, Imperial-Commerce, and Toronto-Dominion, do you, in your university courses in case history methods, write this up and bring it before your students?

Mr. CATERINA: Well, I do not necessarily.

Mr. LIND: No, but is it done generally? Do we not deal with designated areas or some other corporation?

Mr. CATERINA: No, actually to my knowledge only one university is doing this, and that is Harvard University.

The CHAIRMAN: Perhaps Mr. Lind will interject, representing, as he does, London's University of Western Ontario—

Mr. CATERINA: No, this is only a competitor.

The CHAIRMAN:—which prides itself on using the case technique.

Mr. CATERINA: They have some good people; Mr. Martin, and Caleb Williamson, but they have not touched on the banks.

Mr. LIND: Why not, is there not enough disclosure?

Mr. CATERINA: What do you write sir. What are you permitted to write about? Do you make it up, or do you find it?

Mr. LIND: That is what I wanted to hear you say: Thank you.

(Translation)

The CHAIRMAN: Mr. Latulippe, do you have any general questions to put?

Mr. LATULIPPE: If we are on general matters for the moment.

The CHAIRMAN: You must have some questions to put on that statement?

Mr. LATULIPPE: Professor Caterina stated a while ago that the position of banks was not very good. Does he think that the position of the people is better?

*(English)*

Mr. CATERINA: I am sorry, I missed part of the question.

*(Translation)*

Mr. LATULIPPE: Mr. Caterina stated a while ago that the banking situation was not too good. Is the position of the people any better?

The CHAIRMAN: I do not think that is exactly what Professor Caterina was saying. He did not say, I believe, that the position of the banks was not good. He was speaking of the system of disclosure of the financial position. He was not speaking of the financial position of the banks themselves.

Mr. LATULIPPE: Well, that is probably a hypothetical question at any rate. I would now ask the Professor to tell me if he claims that public property should be put on a different footing than private property.

The CHAIRMAN: Do you think that you can comment on that? It might not, of course, be in the area of your studies, so you need not answer.

Mr. LATULIPPE: I do not think the Professor has understood the question. Should public property be treated differently than private property?

*(English)*

Mr. CATERINA: If you will speak slowly, I may understand your French; speak slowly.

*(Translation)*

Mr. LATULIPPE: Should public property, public goods, pay the same rate of interest as private property when it comes to financing?

*(English)*

Mr. CATERINA: All right, dealing with public goods and private goods; is that it?

Mr. LATULIPPE: Yes.

Mr. CATERINA: Treated differently in which way?

*(Translation)*

The CHAIRMAN: Do you have any more questions?

Mr. LATULIPPE: Yes. Do you feel that the balance between production and the volume of money in circulation actually exists?

*(English)*

Mr. CATERINA: I am afraid I cannot answer that.

*(Translation)*

The CHAIRMAN: Professor Caterina is a professor of accounting.



Mr. LATULIPPE: I will put one more elementary question. If this professor teaches economics. . .

The CHAIRMAN: He has just said that he teaches accounting. This is a rather specialized area.

Mr. LATULIPPE: Well, then, I will deal with accounting. Could you tell us this sir. If there are only \$2,600,000,000 of Canada bank notes in circulation, and if chartered banks have \$10,000,000 in deposits in Canadian currency, how is it that they can have these \$10,000,000,000 payable on demand? That is what I would like to know. That is what the people do not understand generally.

The CHAIRMAN: Mr. Latulippe, your question is more or less in order if we consider the whole banking situation generally. However, if we refer here to a topic which is dealt with in our witness' brief this morning, it does not appear that this matter is properly in order. This is a really broad question that you have just put. You have just put a question on the banking situation generally. What the witness has come here to discuss with us is a much more restricted matter; that is, the matter of disclosure of financial information by the banks, etc., on an annual basis. You might reserve your question until we get the Governor of the Bank of Canada back before us.

Mr. LATULIPPE: Yes, of course, I could do that. But what I would simply like to know is—with \$2,600,000,000, we can pay \$10,000,000,000...

The CHAIRMAN: This is a very interesting question of course, but it has nothing really to do with the matters which are dealt with in Professor Caterina's brief. Now, we have decided as a committee to discuss only those topics which appear in the brief submitted by the witness.

Mr. LATULIPPE: It is rather difficult to remain within the context. You spoke of general questions a while ago, did you not?

The CHAIRMAN: We have a witness who might be a professor, but he is a very specialized professor.

*(English)*

Mr. CATERINA: I am not an economist, sir, I do not know.

*(Translation)*

Mr. LATULIPPE: Do you admit, Sir,—I will put my question in another way—that all the work carried out in agriculture and industry, all the work carried out in this country, is adequate to satisfy the needs of the people? Do you feel that all that can be produced by agriculture and industry in this country is enough to satisfy the needs of the people?

The CHAIRMAN: I am sorry to interrupt you once again, but I do think that we should have a little bit of order in our questioning. I think we should remain within the rather close confines of those matters which have been dealt with by our witness. He has not come here to discuss general economic questions. Your questions are in order, of course, generally, within the context of our discussions of the banking system in this country, but Professor Caterina has come here to deal with very narrow topics. He has come here very kindly to put forward suggestions with regard to some very specific improvements.

Mr. LATULIPPE: Mr. Chairman, I do not believe I have received his brief. Would you have his brief in French?

The CHAIRMAN: That is a question which I would put in the hands of our clerk.

Mr. LATULIPPE: If I had the brief of course, I could put questions.

The CHAIRMAN: Generally, the briefs are distributed a few days before the sitting. I will look into this matter with our clerk to find out what happened with the copies of this brief.

Mr. CLERMONT: Mr. Latulippe spoke of a brief in French. As far as I am concerned, I received the Professor's brief in English. I do not believe that our clerk has sent along French copies.

The CHAIRMAN: I will look into the matter because I feel that the Bureau for Translations will have had translation work to do for us. In the available time, perhaps we could continue, this morning or this afternoon, to put questions to the Professor. These are very interesting suggestions which have just been put forward with regard to banking. In the steering committee we could possibly discuss this very important matter. I have not said it is not a very important matter. I am a little sorry to note that we do not have these translations for our French-speaking colleagues.

Mr. LATULIPPE: I have not received that. If it were possible in future to get them, it would be very good.

The CHAIRMAN: Yes, I thank Mr. Clermont for having raised the question, and I want to indicate that I will ask the clerk to send notices as soon as possible to have a meeting of the steering committee to-morrow, and we can then begin to draft our schedule of meetings for January. The matter of copies of briefs in French will have a high priority at our discussions tomorrow. Mr. Clermont might perhaps come to the sitting.

*(English)*

Yes, we should. I was going to mention at the conclusion of our meeting this morning that inadvertently I did not ask the Clerk to send out a notice yesterday, but I think we should try and have the steering committee meeting some time tomorrow to begin planning our agenda for January, at least in a tentative fashion, so that the Clerk can get to work contacting the people, and so on. I feel that this question of translation of briefs should have a high priority place at any meeting we have tomorrow and that Mr. Clermont should attend, either himself or in substitution for one of the government supporters, to join in the discussion of that item. Would you be willing to do that, Mr. Clermont?

Mr. CLERMONT: Yes, I would, sir.

The CHAIRMAN: Because I think this is very important. I am just suggesting that rather than go into this in detail at this time, we should, perhaps, try to complete our discussion with Professor Caterina.

We are having a meeting this afternoon and as you know, our witness is the Canadian Credit Men's Association. They have a more limited area they wish to cover with us. I am wondering, professor, if you have a little time this

afternoon, and if we cannot complete our questions by 1 o'clock, whether you might be with us for at least a short period at 3.45. Would that be possible?

Mr. CATERINA: Yes, I guess so.

The CHAIRMAN: If that is the case, perhaps we can continue, at least, for a while, before adjourning for lunch. If we have completed the questions of a more general nature, let us move along and consider the portion of Professor Caterina's brief headed Assets.

First of all, do we have any further questions on the item headed Securities Investments?

Mr. CLERMONT: On page, 5 items 6, 7 and 8. professor, you say:

For shareholders, excessive liquidity of the investments portfolio can be as bad as lack of it if liquidity is maintained at the expense of profitability.

What do you mean by that? Do you think that banks have not made enough profit, up to now, on their investments?

Mr. CATERINA: No, sir, It is fair to say that any financial manager, be he a banker or one with an industrial corporation, has the task of maintaining liquidity, at the same time, without sacrificing profitability. What I mean is this. Suppose we had a treasurer who was happy to have cash on hand that would pay all of his bills when he wished to pay them. Now, this idle cash would not earn any profits, any interest. It would be idle cash and, therefore, liquidity would be maintained at the expense of good profitability. Let us turn the case around; a corporation treasurer who is very eager to make every penny count and, therefore ties up all of the liquid resources of the firm, be it a bank or Massey-Ferguson, shall we say, then, in this case, the corporation could find itself in difficulty because of inability to pay its bills. So in a sense, really, the real skill of financial management lies in the balancing of liquidity and profitability.

Mr. CLERMONT: And, professor, you would be satisfied if the bank statement showed their investment, as you suggested, for instance, under one year, one to two years, and so on.

Mr. CATERINA: I believe so. Even that liquidity is a very difficult element in a bank's portfolio especially.

Mr. CLERMONT: Would you be satisfied, as you have suggested, federal government, provincial government and others.

Mr. CATERINA: Yes.

Mr. CLERMONT: You would be satisfied with others, no distinction between commercial or any other.

Mr. CATERINA: What I am concerned with is the principle of that, not the details. As of now we have in fact the amendments to the bill, schedule N. Here we have different types of securities at amortized value. There is no indication of maturity at all. So we do not know really, how liquid the bank portfolio is.

The CHAIRMAN: Maturity is the key.



Mr. CATERINA: Very much so, to my mind it is. I am sure that banks that are well managed do have a proper liquidity, but no one has an indication of that really.

The CHAIRMAN: Any further question on this?

Mr. CAMERON: (*Nanaimo-Cowichan-The Islands*): Professor Caterina, do you agree with the new provision in the bank bill that for the first time places the secondary reserves on a legislative basis that is now mandatory, instead of the arrangement which was made between the central bank and the banks some years ago for the maintenance of liquidity.

Mr. CATERINA: Again, may I decline to answer that. It raises another question really. In item one of the new schedule in the amendment, we have cash and due from banks. In the bill that item is broken down into three parts. And again, is it an improvement? Well, yes, and no. The economists might not like it, because this item now may not allow them to guess at the amount of free reserves that the banks have; whereas before they could, but as an accountant, shall we say, I am not overly concerned, except for one thing; To the extent that deposit with the central bank is frozen in a real sense, they are not part of a bank's liquid resources and from that point of view, I would suggest, perhaps, a return to the previous schedule N where notes and deposits with the Bank of Canada were shown separate from deposits with other banks. But if I could predicate it on the concept of liquidity—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): This is on the concept of liquidity, the establishment on a legislative basis of the maintenance of certain stipulated ratios of liquidity, which is a new departure.

Mr. CATERINA: I would not volunteer to comment on that.

The CHAIRMAN: If there are no further questions on the item headed Securities Investments—

(*Translation*)

Mr. LATULIPPE: I have a supplementary question. We discuss reserves. . .

The CHAIRMAN: We are not speaking of reserves. Mr. Cameron has tried to establish the relationship between the reserves question with the method of reporting on the matter of liquidity.

Mr. LATULIPPE: There is mention of liquidity.

The CHAIRMAN: But only in the context of financial reports.

Mr. LATULIPPE: If the banks were to maintain a certain liquidity, how can they maintain liquidity when they have to deposit one billion eight hundred and seventy-four million in reserves with the bank out of two billion six hundred million? This does not favour the public interest. Something is not working out right.

The CHAIRMAN: The witness has just noted that he is professor of accounting and not a professor of economics. I do not think he would like to try to answer that question, interesting as it is.

(English)

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The basis of my question was the professor's reference to the possible conflict between profitability and liquidity considerations.

The CHAIRMAN: In fact at the moment we really are trying to analyse in a closer fashion the rather narrow and technical point, although an important point, that he just raised with respect to the financial reports of the bank.

Now, let us see if we can at least deal with item 11: Other Loans less Provisions for Estimated Loss, before recessing for lunch. Are there any further questions on this specific item in Professor Caterina's initial brief. He has already reviewed it with us in a general way. Mr. Clermont has been kind enough to raise that with us and explore that for us in his own questioning. Are there further questions on this point at this time? As far as the technique of reporting is concerned it is simply a matter of distinguishing between the two types of loans under the two headings on the assets side.

If that is the case, we can ask if there are further questions on item 13: Securities of and Loans to Corporations Controlled by the Bank, and again I think we have already had a preliminary discussion.

Mr. GILBERT: Professor Caterina, in this section you are asking that controlled corporations that are not consolidated should give a full accounting. I am sorry, you are asking for controlled corporations which are consolidated, or is it not consolidated.

Mr. CATERINA: Not consolidated.

Mr. GILBERT: All right. What corporations are you referring to?

Mr. CATERINA: Under the Bank Act, only subsidiary banking corporations may be included in the statement of the parent or major bank, shall we say.

Mr. GILBERT: Let us take RoyNat.

Mr. CATERINA: RoyNat is a non-bank; under the bank act that would not be consolidated.

Mr. GILBERT: That is right.

Mr. CATERINA: Likewise, shall we say, the realty companies that banks control fully. Now these companies will not be consolidated because the Bank Act says that the operations are so different from those of the bank that no useful purpose may be served by consolidating them.

The CHAIRMAN: They do have to have their own statement.

Mr. CATERINA: Yes, again the Bank Act, and the bill as well, require that for controlled companies, which are not consolidated, the bank must show the amount at which this investment is carried, and also a statement of financial position of each of the major controlled corporations. My argument here is not with what is required, but with what is not required, in the sense that banks do have these controlled corporations whose assets they show through statements of the controlled corporation. The amount at which they are shown in the books of the company is also stated in the budget of the bank. But what about the flow of profit from these to the bank. There is no indication anywhere, sir, and this allows me to say, we do not know.

Mr. GILBERT: In other words, you cannot determine the quality of the management.

Mr. CATERINA: No, that is not it. I cannot determine how much of the bank's profits have come from controlled corporations and how much from bank corporations.

Mr. GILBERT: Oh, I see. I get your point.

Mr. CATERINA: This is a very crucial point to my mind.

Mr. LAMBERT: In view of the amendments to the Bank Act which will require banks to spin off their holdings in these non-banking institutions, with the exception of the service corporations, they will no longer control.

Mr. CATERINA: Well, if this is the case, there would be no problem then.

Mr. LAMBERT: Well, that is all right.

Mr. CATERINA: But as of now we have not.

The CHAIRMAN: Does the Committee wish to sit for another few moments to detail with the last item under the heading "Assets"?

Mr. CLERMONT: Regarding the control of other companies by the banks, here I have the Bank of Montreal's annual statement for the year 1965, and they show "statement of company belonging to the bank"; is that what you have in mind—

The CHAIRMAN: Yes.

Mr. CLERMONT: —or is it something like RoyNat?

Mr. CATERINA: Would you please indicate which statement of which company?

Mr. CLERMONT: The Bank of Montreal Realty Limited.

Mr. CATERINA: O.K. That is all right.

Mr. CLERMONT: And the other one is the Bank of Montreal Trust Company.

Mr. CATERINA: Yes. Now, these two companies are controlled by the Bank of Montreal.

Mr. CLERMONT: They say "owned".

Mr. CATERINA: "Owned", fine. It is even more than that. Although we know in each case what assets and liabilities each of them has, we are not told how much of the profits of these companies have been transferred from them to the bank because there is no statement of profit or loss for the controlled corporations that it owns.

The CHAIRMAN: Thank you, Mr. Clermont. Does the Committee wish to deal with the final item under the heading "Assets" before we recess for lunch, and leave the discussion of individual items under "Liabilities" for this afternoon's sitting?

Mr. GILBERT: I think the Professor dealt with that.

The CHAIRMAN: I am just wondering if there are any further questions. It is true he did deal with that item quite thoroughly. Are there any further questions



on this proposal with regard to reporting of acceptances, guarantees, and letters of credit? If not, I think we will recess until 3.45 p.m., and at that time the Vice-Chairman, Mr. Laflamme, will be in the chair and we will complete our discussion with Professor Caterina, following which you will hear from the Canadian credit men.

I want to thank you personally, professor, for your most stimulating presentation.

This meeting is recessed until 3.45 p.m.

#### AFTERNOON SITTING

The VICE CHAIRMAN: Gentlemen I call this meeting to order.

I was told by the Chairman that at the adjournment we had reached the third item under discussion, which deals with liabilities, starting at page 9 of the brief presented by Mr. Caterina.

I am ready to recognize any member who will signify his wish to ask questions regarding this item.

Mr. LAMBERT: With regard to the rest account, have you any evidence that at this time any proportion of the rest account that will be paid in by the shareholders is a meaningful amount?

Mr. CATERINA: I can only go by the Bank of Canada figures, and those are the ones in my brief. They give no indication whatsoever for any individual bank.

Mr. LAMBERT: Does it mean anything today?

Mr. CATERINA: Which?

Mr. LAMBERT: If there has been a contribution from the shareholders to the rest account for the chartered banks just what does it mean? Is it meaningful today, in the relative position of the banks?

Mr. CATERINA: I believe it is. To the extent that one wants to segregate capital contributions from an earnings-retained basis then the distinction is very significant. In other words, if you look at the rest account of any one bank we cannot say very much about it—how much of it represents premiums paid in by shareholders and how much of it represents earnings retained in the business by the banks. By all standards of financial reporting the two are kept separate. In other words, capital contributions must be kept separate from other earnings that business may decide to withhold from distribution. This applies to all industrial and commercial corporations, because the Canada Corporations Act requires that for industrial and commercial corporations. We do have, also, publication, by the Canadian Institute of Chartered Accountants, of inquiries, or requests in depth, of its members. So that both the C.I.C.A. and subsections (x), (y), and (z) of section 119 of the Canada Corporations Act require the distinction of all investments in commercial corporations.

Mr. LAMBERT: I will come back to that. I want to make an examination of our more recent statistical table before I continue.

(Translation)

The VICE CHAIRMAN: Mr. Clermont.

Mr. CLERMONT: Mr. Caterina, in your submission—

The VICE CHAIRMAN: Could you wait for a moment, Mr. Clermont?

Mr. CLERMONT: In your brief dealing with Bill C-222, page 2, you state and I quote:

(English)

In connection with the accumulated appropriations for losses on loans and investments, it should be indicated whether they represent the maximum amount permitted under the Income Tax Act and Regulations.

(Translation)

What do you mean by this quotation, because I imagine the banks must take everything the Law permits them to take.

(English)

Mr. CATERINA: My guess would be that they do that, and if they do not we are very sympathetic about their position, shall we say. They should. It is good business.

However, the point is this, that although nearly all banks may take advantage of the full allowance under the income tax regulations, some may not. Therefore, for those whose allowances are below, shall we say, the income tax maximum, there is a future benefit to be derived in terms of the greater allowance that they may get later on. To put it another way, sir, are the allowances calculated on the basis of business judgment, or on the basis of maximum tax benefit, or both? I presume that they are on the basis of maximum tax benefit. It is only fair to assume that.

(Translation)

Mr. CLERMONT: On page 14 of your brief dealing with Bill C-102, an example is given of a United States bank which was on the market for bonds and in the interval it was informed they would have a loss of so many dollars following exchange transactions, the authorities of the bank asked for advice from their legal advisors and decided to make public, by circular letter, the amount of this loss. Would you suggest to this Committee that losses or reserves, or general reserves and hidden reserves all be indicated? Do you want the banks to make public a total sum indicating the reserves, or in other words, do you want the banks to indicate a total for all the banks taken together or do you want each bank to list its own reserves?

(English)

Mr. CATERINA: Sir, the example I give on page 14 of the submission is an indication of the extent to which full disclosure has become possible and acceptable in the United States. It is an example to support the views I expressed previously.

My suggestions are based on disclosures by each individual bank and not by the system, because we already know what the system as a whole has. What we do not know is what each individual bank has in terms of reserves.

Mr. CLERMONT: But would you be interested to know only the reserve, or the loss every year?

Mr. CATERINA: Well, we are going a step further perhaps. Shall I proceed?

The CHAIRMAN: Yes, go ahead.

Mr. CATERINA: If we can carry on in this fashion perhaps we may elaborate on this. If the operating statements of the banks are to fulfil the objectives assigned to them, that is, to show operating performance, then, in my judgment, losses which banks may sustain either on their loans or on security investments, do represent a cost of doing business, and, as such, they should be disclosed in their operating statement.

The amendment to the bill has schedule "O", the amended one, and schedule "P". In schedule "O" we do have an item called "other operating expenses", including the reason for losses on loans based on a five year average loss experience. That would likely be an operating loss, you might say, or cost of the loan business. If we feel—and I submit it is felt—that such information is significant to assess the bank's operating performance, then it ought to be shown as such, and not buried in the total of other operating expenses.

The whole point is: How significant is it? If this is significant, then I suppose the managements of the various banks may be judged, on their loans performance, by the amount of the provision charged off to operations. What we have now is this portion that is hidden here, and then in schedule "P" we do have another portion left over—item number 3. Item number 3 is the excess of loans provision under the regulations, and what is perhaps required from management is a meaningful costable period which is included in schedule "O"; so that the sum of the two, shall we say, would represent the maximum total provisions that banks would be allowed.

Now, in my judgment, either schedule "P" or schedule "O" ought to indicate the proportion of the total provision which management has deemed to be the cost of doing loans each year.

*(Translation)*

Mr. CLERMONT: Do the representatives of the Canadian Bankers' Association who came before this Committee,—I am under the impression that the representatives objected to providing the information which Bill C-222 and amendments thereto require, because they claim that if a bank were to suffer substantial loss in a year there might be public lack of confidence. What is your reaction? Does the Canadian Government's proposed Bill to be tabled in Parliament for deposit insurance, is this a means of encouraging public trust in the banks?

*(English)*

Mr. CATERINA: I would not suggest that, because what I am driving at here is to have as clear a picture of banks operating performance as is reasonable.

Deposit insurance will, I suppose, protect the depositors against losses that they might sustain if the bank should run into difficulties, but that will not overcome the problem of the shareholders' inability to assess how well or otherwise the bank has run its loans portfolio. To the extent, I repeat, that loans are a significant portion of bank assets, their costs directly related to their operations ought to be disclosed.



(Translation)

Mr. CLERMONT: Thank you, Mr. Chairman, that is all.

(English)

The VICE CHAIRMAN: Does anyone else have questions?

I will now ask Mr. Caterina if he has any other comments he wishes to make in conclusion.

Mr. CATERINA: Yes, I have two or three, Mr. Chairman.

Mr. CLERMONT: Mr. Chairman, if no one else has a question, I would like to ask one. On page 18 the professor says:

I strongly recommend that this Committee take into consideration the possibility of submitting the financial reports of banks to an impartial review by a court—

What have you in mind there and what about the position of the Inspector General who is doing this today?

Mr. CATERINA: The interests of the Inspector General of Banks are not identical to those of shareholders, or, perhaps, even of depositors. The inspector of banks is charged under the act to perform certain specific duties and one of them is not to see to it that the fairest presentation of the banks' operating results and financial position be given at any one point of time. If I am wrong, I stand to be corrected. I am not too sure that the inspector is charged with this responsibility.

Mr. SCOTT: Not unless it is a case where there is any specific responsibility.

Mr. CATERINA: No. Even then the inspection of banks does do a very efficient job, but it is within his sphere of competence, and given that the banks have been reluctant to date to do anything more than make a disclosure of a minimum of information—perhaps it has been conspicuous more for its lack of information to date—and if my ideas are so unattainable, then I have a suggestion to make. As perhaps you are aware, the Canada Corporations Act, 1965, has a new provision in it whereby a corporation which refuses to disclose its sales figures has to show cause to a judge why it should not do so. With this provision which is now inserted in the Canada Corporations Act, where you have the judiciary deciding, then if what I am suggesting here is not acceptable, or is not consistent with what is being done elsewhere in the same field, that is one solution. This is the meaning of the recommendation there.

Mr. MORE (*Regina City*): So long as the law does not require it what purpose could the Committee serve.

Mr. CATERINA: Which committee have you in mind, Mr. More?

Mr. MORE (*Regina City*): Your reference is that this Committee take into consideration the possibility of submitting the financial reports of banks to an impartial review by a court. If they comply with the law what is the question that the court has to decide?

Mr. CATERINA: On whether or not the statements, which are a full reflection of various requirements, represent fairly the financial position and the operating performance of the banks.

Mr. MORE (*Regina City*): Do you think the courts are a judge of that?

Mr. CATERINA: Why not?

Mr. LAMBERT: This is the point that bothers me, too. The court has to interpret the law. Is it realistic to assume that a judge, or the court, or at whatever level you want to set it—you might want to go to the Exchequer Court—would substitute his discretion and his business acumen for that of the boards of the various banks which might be up for reference? I find that a bit difficult, Professor Caterina. A court would simply say: "This is not our purpose", and refuse to do so.

Mr. CATERINA: This may well be the case.

Mr. MORE (*Regina City*): You might call this a Committee of inquiry, and you sell your case to the Committee, with a recommendation that this be the law—

Mr. CATERINA: Mr. Lambert's point is well taken, and the only order of reference I can give is the one I have just mentioned in the 1965 Canada Corporations Act. Would a judge, whichever court he may belong to, be qualified to determine whether the disclosing of sales of a corporation would be detrimental to the corporation and would he be in a better position than the board of the firm which is against it.

Mr. LAMBERT: I forget the provisions of the act, although we passed it last year, but it requires disclosure in certain sensitive fields, and there is an obligation; and then the company says: "We do not want to disclose this information." There is a review of certain circumstances which might justify a company's not disclosing its figures.

This is not what you are asking for here. I do not know at what level we would have to set it in an act for a court to enforce it.

The burden is reversed in the Canada Corporations Act. The figures are required, but if there is some very valid reason, such as disclosure to competitors or to foreign corporations, or that it may affect security of the state in some way or another, a company can come to court and seek relief against it. It is a principle which is quite different from the one applied here.

Mr. CATERINA: It could very well be; but my assumption is that a question of fairness could be decided by a court. I am not a lawyer, and perhaps I am stepping in quicksand right now—

Mr. MORE (*Regina City*): Yes, Professor; but in the one case the banks are fully complying with the law, and on that there has been general agreement.

Mr. CATERINA: Yes.

Mr. MORE (*Regina City*): So that the law requires nothing of them; there is no issue for the court to decide. They are complying with the law.

In the other case the law offers relief, providing they are judged to have a valid reason for seeking relief. That is determined by the court and if it is found that they should have this relief the court grants it.

There is nothing here for the court to deal with, because they are complying with the law.

The VICE-CHAIRMAN: I do not want to interrupt the question or the answer but I do not think there is much to be gained in trying to find out how a court should be established to decide or analyse statements from banks.

Mr. LAMBERT: On the other hand, Mr. Chairman, I think you will agree that if the witness has a certain opinion we should examine his thinking in regard to it because he may have a perfectly valid point. If he can convince this Committee of the validity of his point, that is all to the good, and we will have made some progress.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I would think, Mr. Chairman, that what Professor Caterina is really seeking is to have an enquiry to—how does he put it here?—declare whether the disclosures are reasonable and fair in the light of prevailing circumstances. I would suggest to Professor Caterina that it would have to be a court of enquiry composed of chartered accountants like himself.

Mr. MORE (*Regina City*): Would you not agree that the Porter Commission has been rather a court of enquiry, Mr. Cameron?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes; that is so; but they made no judgment on this bill.

Mr. CLERMONT: Personally for me it would be an interpretation, because if Parliament passed a law I am sure that the Department of the Inspector General would see to it that the banks followed the law; and I do not see another Board doing the same work.

Mr. GILBERT: Professor Caterina have you in mind that we put a clause in the bill which would refer the financial statements to the court for review?

Mr. CATERINA: No there is not one—

Mr. GILBERT: But that is not what you have in mind. You have to have some authority to refer to a court.

Mr. CATERINA: Yes.

Mr. GILBERT: As you pointed out in the Canada Corporations Act there is authority, because there are requirements about disclosure and failure to do so. That gives the court the authority to review. This is the type of machinery that we would have to build up in order to obtain the result that you have in mind.

Mr. CATERINA: No; my entire point here, gentlemen, is that the reports of the banks do not comply with current standards of reporting for the economy as a whole. This is the point of issue here, and I hope I have shown throughout the reasons for my position. I may well be taking an extreme position, but if my views are completely out of line, then let us have an impartial body look at these papers and see whether they are consistent with current requirements in financial reporting by other institutions. This is the entire point I am trying to make here.

Mr. LAMBERT: Mr. Chairman, may I pursue that? One would have to justify reasons for the changes to be made. I would suggest that merely to change for the sake of change is meaningless. However, if, as a result of the changes which you would seek to have, one could make a more meaningful analysis of the banks' operations, with an improvement of the banks' operations—and I think that would be in the public's interest—then I would go along with you.



If, on the other hand, it is merely to have more information because of interest in the operations of banks, or to be an academic exercise on which a lot of people and financial writers can speculate or talk, or write, then I am not quite so sure that this is worth while.

Thirdly, can it be shown that the investing public and the Canadian public have suffered in the past because of the standard of financial reporting that the banks have engaged in? Have any losses been suffered? These would be the questions that I would feel would have to be answered, in the affirmative, in order to justify it.

Mind you, I am somewhat in sympathy with some of your statements—for example, the one about the published statements on the whole of the nature of the holdings of securities. I am sure that the banks have this information. If you look at the statistical summaries you can see there the nature of the quarterly classification of general loans—personal, farmers, business, public utilities, construction contractors, merchandisers; all the information is there for the banks as a whole. You want it for each individual bank. If they have provided the Bank of Canada with this information, they have it. In certain sectors I agree with you. I certainly would like to see in a bank report an additional statement about the currency of their security holdings, and that sort of thing.

The VICE-CHAIRMAN: Were you finished Mr. Lambert?

Mr. LAMBERT: Yes.

Mr. LEBOE: Mr. Chairman, I think Professor Caterina was also enunciating the principle that what is fair for one is fair for the other. I think we must not lose sight of principle. One of the basic foundations of our whole society is the application of principles generally, in justice and fairness, to the various individuals to whom the principles apply.

Professor Caterina can correct me if I am wrong, but I think that what he has in mind is the principle of the banks not being put in a special classification by themselves in connection with this type of reporting. Am I right?

Mr. CATERINA: Very much so, yes.

Mr. CLERMONT: On page 17, in the concluding remarks, there is one question that puzzles me, where the Professor has stated:

The government virtually underwrites its solvency.  
—that is the banking industry.

The VICE-CHAIRMAN: What is your question, Mr. Clermont?

Mr. CLERMONT: What does Professor Caterina mean by “virtually underwrites its solvency”.

Mr. CATERINA: What I have in mind there, sir, is that the operations of certain government institutions can be so geared as to prevent a bank from going bankrupt. Let us put it that way.

Mr. CLERMONT: Which we all hope will not occur.

Mr. CATERINA: I think we can take that for granted. To the extent that certain government agencies are geared to bail them out, so to speak—to put it in very crude terms—if these institutions should get into difficulty, as I say,

solvency is virtually guaranteed. Mind you, there is no law saying that they have to do that. Perhaps you will allow me one more comment, sir. There is another example of what I mean. You may recall that at the time of the Atlantic Acceptance collapse last June, the Bank of Canada came out with a very innocuous statement indicating that it, the Bank of Canada, would make available reserves to chartered banks for legitimate business purposes loans to sales finance companies. This was just a three-line statement.

What did the Bank of Canada have in mind there? No one knows; but the fact that the Bank of Canada came out with the proposition that it would make available more reserves to commercial banks to, shall we say, help sales finance companies, which were found in a rather shaky position, leads me to the assumption of a virtual guarantee of solvency.

Mr. GILBERT: I wonder if Professor Caterina would turn to the sample, as he called it this morning, of the First National Bank and its statement of operating earnings, which follows page 19, and compare it with schedule "O" of the bank bill.

Is the statement of operating earnings of the First National Bank of Chicago preferable to schedule "O"? Is this the type of statement that the shareholders should obtain?

Mr. CATERINA: Well, I think the two are substantially the same.

Mr. GILBERT: But do you think that the statement of the First National Bank is more revealing to shareholders than is schedule "O"?

Mr. CATERINA: Well, schedule "O" was not available at the time I wrote that.

Mr. GILBERT: Oh, I see.

Mr. CATERINA: The schedule is about six weeks old.

Mr. GILBERT: I do not see any balance sheet for the sample that you have, whereas we have section (n). Are you suggesting that a balance sheet is not necessary, or should we—

Mr. CATERINA: No. All I am suggesting there is that the balance sheet of this bank was substantially the same as those of other banks. There was no point in reproducing it.

Mr. GILBERT: Oh, I see.

Mr. CATERINA: I have followed the principle of including exceptional information rather than like information.

Mr. GILBERT: Oh, I see. I thought you were suggesting that they not file a balance sheet.

Mr. CATERINA: Oh, no. All I am doing in this case is giving an example of an operating report.

Mr. GILBERT: Then would you suggest another schedule for the summary of changes in their own reserves, which is dealt with further on?

Mr. CATERINA: It is just a question of choice, because we would have schedule "P", in a sense. Its function is that, really.

Mr. GILBERT: Do you think schedule "P" is now sufficient?

Mr. CATERINA: I think so.

Mr. GILBERT: It is sufficient.

Mr. CATERINA: I think so. There are a couple of things there. I am seeing this licence for the first time, and I was just scribbling some notes on it. Is that all right?

First of all, as I suggested this morning, I would like to see a disclosure, either in schedule "P" or schedule "O", of the total provision for loan losses on the basis of five years' average loss by the banks.

Mr. GILBERT: That is in.

Mr. CATERINA: I beg your pardon.

Mr. GILBERT: That is in the proposed amendment.

Mr. CATERINA: I know; but you show a portion of it in schedule "P" and a portion in schedule "O"?

Mr. GILBERT: Are you looking at the amendments that Mr. Elderkin proposed?

Mr. CATERINA: Yes. I have the one dated October 25th.

Mr. GILBERT: That is all.

Mr. CATERINA: Yes. Now, as I read them, sir, in schedule "O", in the last item under expenses, we have operating expenses including provision for losses on loans based on a five-year average loss experience. Then on schedule "P", item number 3, we have loss experience on loans, less provision included in other operating expenses.

Mr. LAMBERT: You want that total.

Mr. CATERINA: Either that, or an indication somewhere of the amount charged to operations. Your information is there all right, but one cannot put it together. It is split.

Mr. GILBERT: I think that is all, Mr. Chairman.

The VICE-CHAIRMAN: Thank you, Mr. Gilbert. If there are no further questions—

Mr. LAMBERT: I want some explanation. Perhaps we can get some help from the Inspector General's office, but in schedule "O" there is an item under operating expenses including this provision for losses on loans based on the five-year average; then there is a further item called "Appropriation for losses". In schedule "P" the reference is to loss experience on loans, less the provision included in other operating expenses; so that item 3 becomes appropriation for losses.

Mr. CATERINA: Item 3.

Mr. LAMBERT: Item 3 in schedule "P" seems to me to be the item called "Appropriation for losses" in schedule "O".

Mr. CATERINA: No, I think it is Item 2, sir. Item 2 of schedule "P" would be the appropriation for losses in schedule "O". I am just guessing at this.

Mr. LAMBERT: This is what I would like to have cleared up.



Mr. W. E. SCOTT (*Assistant Inspector General of Banks*): I think that the figure for "appropriation for losses" in schedule "O" is the balance transferred inside to reserves, over and above the amount buried in other operating expenses. Therefore I think Mr. Caterina is right when he says that the schedule does not permit you to see the total amount put aside specifically to meet losses in the current year.

Mr. LAMBERT: That helps to clarify it.

Mr. CATERINA: Mine was just a guess.

(Translation)

The VICE-CHAIRMAN: Mr. Latulippe, would you have any questions to put?

Mr. LATULIPPE: I would have a few questions to put with regard to reserves. It is said that banks have reserves which are designed to provide against the possible loss. According to the financial statements, these losses are  $\frac{1}{2}$  and 1 per cent approximately. There is not one company in Canada which loses as little. The business which loses the least in its investments or loans is the banks. The bank runs almost no risks whatever. When a borrower borrows he provides the securities. When a customer is not a good customer, another person is required to endorse the loan otherwise the borrower gets no loan. We are afraid of bank bankruptcies, we attempt to set up rules to prevent banks from going into an insolvency. Banks are the strongest institutions in Canada. Banks are those institutions which enjoy the greatest possible advantages in the country. They can create credit, they can distribute credit, they multiply Government bonds ad infinitum. With Government bonds they can lend any amount of money, therefore, it can be said that banks are in a very strong position. We need not worry about the possible failure of banks because the present legislation is such that they are protected to the greatest possible degree, all Canadians are protected. This being said, I would like to say that I have no objection to these institutions being as solid as possible. I have no objection to banks making a profit and being prosperous. In fact I have no objection to them having reserves. I would only ask one other thing—we should have the same type of operation for persons or families. The formula income expense profit should be applied to persons and families. I think the ills of our economy are not to be looked for in institutions, it should be looked for in the spirit of our legislators, which always seeks to protect capital instead of protecting the people of this country, who are the sinus for this institution. That is my point, Mr. Chairman.

The discussion we should be having at this time is this. These financial institutions should be at the service of the population. They render a great service, but they can render greater service still because at the present time the economic life blood of society is not circulating as it should.

The VICE-CHAIRMAN: Mr. Latulippe I did allow you to some extent to express an idea which you had. I would like to remind you that you might have another opportunity at some future time to return to this. If you have any opinion to express about banks generally you will have an opportunity to do so when the bank people will be back before the Committee, and you will have every possible opportunity at that time to make remarks on that subject. However, as Chairman of this Committee, I unfortunately feel I must remind you that we are questioning a witness who has introduced a brief dealing with

some very narrow points. His brief deals with financial statements which, according to him should represent as clearly as possible, the actual financial position of the bank. I do not think you should go any further in the present expression of opinions you have on banking institutions generally. However, if you have an additional question to put to Mr. Caterina concerning the matter of banking obligations, banking statements, etc., which are at present under discussion, I would be quite willing to entertain your questions. But for the moment, I must interrupt you because of the rules of our Committee because the same general rule should be applied to all members, because if somebody starts expressing his own opinion, it will provide each and every one of us with the opportunity of making a speech, and we will be not much further ahead tonight.

Mr. LATULIPPE: With regard to reserves, hidden reserves, secret reserves or what have you, I would like to know this. I have not had an opportunity to read your report. I received it a little late this afternoon and it is in English, and I have a little trouble understanding the whole thing, all the terms he uses, but I felt that he was saying a great deal about reserves, about hidden reserves, and general reserves. I know that everybody knows that banks have reserves. What would the professor suggest that we put into the reserves. I believe that you had suggested that a Committee be set up to decide about these matters but here again we are faced with the same position. We give all rights and all privileges to these institutions, and any Committee that could be set up could not go beyond the rights given to these institutions by Parliament. I think legislation should be amended in such a way that such a Committee have a definite terms of reference in this way. If we go on as we have been going on up to now, this Committee will have really nothing to do, but I believe that there is no need for this. The legislators took the responsibility, if legislators were willing to look for proper solutions we would not need such a Committee.

*(English)*

The VICE-CHAIRMAN: Mr. Caterina, I now have the great pleasure, on behalf of every member, of thanking you very much for your support and for the important observations you have made during the day. I am sure everyone shares my view, and that we all appreciate your interesting remarks.

Mr. LAMBERT: There is one aspect that I want to discuss just a little further.

Do you think there would be anything to gain by trying to achieve greater uniformity in fiscal year-ends as between government, industry and business, again really for purposes of comparison? I realize that there are many difficulties with regard to this; that with businesses because of their particular nature, it is far more practical for some to have the year end at the end of January and others at other times.

The government, it seems to me, comes in at an odd time, March 31st. When you want to compare the operations, say, of government, across the nation, with industry and with business, you have periods of overlap which, to me, present some difficulty in the making of a meaningful comparison. What is your experience in this regard, and have you any ideas?

Mr. CATERINA: The ideas I have sir, are that perhaps it would not be feasible to have common year-ends for all, for the basic reason that if there is a natural

period when operations are at their lowest that is deemed to be the time at which the year-end should fall.

Suppose we were to take an extreme case and have the year end December 22nd for everyone. The department stores would be in chaos because of the inventories which they have then. Or suppose we have the year end for steel companies and automobile companies in January, or in the spring, perhaps, when there is great activity with the new models. In the case of government, I do not know when is the peak period in tax receipts, or taxable payments. Therefore, the decision on year-end is based on this natural flow, you might say. Is there a point in the twelve-month period which best lends itself to accounting for everything?

Mr. LAMBERT: In other words, you feel that the practical difficulties override, shall we say, any efforts to arrive at some uniform period?

Mr. CATERINA: I should imagine so, yes. This I will do: I will endorse your view fully on an industry-by-industry basis; that I would do. But for the country as a whole, perhaps, I would not.

Mr. LAMBERT: Thank you very much.

The VICE-CHAIRMAN: I will now call our next witness, Mr. E. P. C. Burke. Unfortunately I have not had the opportunity of meeting Mr. Burke before, so I cannot say much about him personally except that he is the General Manager of The Canadian Credit Men's Association, Limited.

Mr. Burke, usually witnesses do not read their brief, they summarize it, after which all members have the opportunity of asking questions regarding the representations which are made. I will ask you, then, to summarize your representation.

Mr. E. P. C. BURKE (*General Manager, The Canadian Credit Men's Association Limited*): Mr. Chairman and gentlemen, our brief indicates in considerable detail why the prevailing practice of charging exchange on out-of-town cheques is undesirable in today's business climate. Probably the most important point is that under the law the payer is responsible to see that the payee receives full payment for an indebtedness. Unless par clearance has been set up with the payer's bank, it is necessary for him to add the proper amount of exchange, calculate on whether or not the cheque will be cashed where a branch point of his bank exists. If one does exist, negotiation of such cheques starts with one-eighth of one per cent and a minimum of 15 cents. If no branch of his bank exists, then the rate is one-quarter of one per cent, or a minimum of 25 cents.

It can easily be seen that every cheque issued must be scrutinized and the calculation of appropriate exchange charges made and added to the cheque. The bank where the deposit is made also must check on the accuracy of exchange charges. Unfortunately the custom of the payer issuing cheques for the face value of the debt has become prevalent. When this is done the payee then becomes responsible either to challenge the omission of the exchange or pay it himself.

As indicated in the foregoing, banks have discretionary powers to determine whether certain of their customers are entitled to par clearance or not. We consider this discriminatory.



We specifically draw the attention of the Committee to that part of the royal commission's report on banking and finance on pages 393 and 394 where they recommend that there be a statutory prohibition of charges on the negotiation of out-of-town cheques. They specifically claim that the actual handling of these cheques does not involve any significant cost to the institution concerned.

We draw attention to the observations of the royal commission, which are:

It seems to us unreasonable that the chartered banks should have to negotiate all government cheques without charge to the authorities.

We submit that it is unrealistic and wasteful of manpower that business, industry and individuals find it necessary to scrutinize every cheque deposited to determine whether or not exchange is payable to negotiate the cheque in question. It is equally wasteful of the bank's time to have to scrutinize each cheque to be sure that the exchange has been added and to check the calculation.

From actual observations we have made in certain of our member companies we have established that the actual cost of clerical time involved in examining cheques and computing exchange in many cases exceeds the amount of exchange to be collected. Surely this type of inefficiency must be removed from the conduct of day to day business. You will recall that the royal commission set out that in many European countries par clearance of cheques is an actual fact today. This reduces the paper work of the financial system, cuts down on float and clearing charges—and this is the important point—and assures that the recipient gets the full amount owing to him.

It will be of interest to you to know that closer to home in the United States of America the American Bankers' Association went on record in support of par clearance in 1964, and as of June 30, 1966, 28,183 banks were clearing cheques at par against 1,772 charging exchange. This means that 94.1 per cent of all United States banks have par clearance of cheques.

In conclusion and to summarize, we submit that any system that encourages variance from the intent of the law which places the responsibility for full payment on the payer, any system that is discriminatory, any system that is highly inefficient in the use of manpower, should be removed from the day to day conduct of Canadian business.

The VICE-CHAIRMAN: Thank you very much, Mr. Burke. In listening to the summary presented by Mr. Burke, I think there is one main point which is put before the members, and this is the action of the bank regarding the par clearance of out-of-town cheques and the effects of it. I ask members who wish to ask questions to signify their intention. I recognize Mr. Lambert and then Mr. Wahn.

Mr. LAMBERT: Mr. Burke, I am interested in your observations. Knowing the responsibility between a debtor and a creditor as to the liquidation of a debt, your brief does suggest that the charge made by the bank is conducive to an actual breach of the law. I put it to you that it is not because it is the responsibility of the debtor to pay his debt. If the person who owes a debt goes to the post office and buys a postal note he pays a commission; if he goes to the Canadian National Express and buys a money order he pays a commission, which is the equivalent of a clearing charge, so why is it wrong under those circumstances for the banking system as a whole, on that very narrow point, to make a charge?

Mr. BURKE: On that narrow point, if you go to a post office or an express company they make out the postal note or the order. They perform that service and make a charge for it. An individual in a town has a pad of cheques. He writes his own cheque and, rather than try to compute the amount of exchange, he writes it for the face value of the indebtedness. In the main, this is the practice.

Mr. LAMBERT: Has he heard of the practice of marking his cheque "add exchange"?

Mr. BURKE: Yes, some of them have but unfortunately they ignore it.

Mr. LAMBERT: This is just trying to get somebody else to take the charge.

Mr. BURKE: That is right.

Mr. LAMBERT: On the other hand, what would you think about value dating them? It occurs in Europe and I am just wondering about the example of the United States that you cited. Is the practice of immediate credit given for a cheque, or is value dating now the practice?

Mr. BURKE: I think it is immediate credit, from all I can gather.

Mr. LAMBERT: What would you think of value dating them?

Mr. BURKE: Value dating is not entirely across Europe, is it? According to the royal commission they are using a system where people are assigned numbers and they possibly do not issue a cheque.

Mr. LAMBERT: But are you satisfied that if you had an account in a European bank and you went along and instructed them to pay XY company in City A some distance away, that they would do it without charge?

Mr. BURKE: No, I would not imagine that they would.

Mr. LAMBERT: In other words, the debtor there is actually paying what he should be paying?

Mr. BURKE: That is right.

Mr. LAMBERT: What about compensating the bank for the float that is involved in the clearing of cheques? This is in contradistinction to value dating.

Mr. BURKE: Yes. I think the float problem, from my discussions with bankers, has been considerably reduced with data processing and the fast transfer that is possible under their existing methods. I think it is for this reason that the royal commission commented that there is no significant additional charge or cost to clear out of town cheques at par as opposed to clearing in town cheques at par.

Mr. LAMBERT: Well, to what extent do you estimate that the banking system today uses electronic centralized computing systems which permit a significant cut-down in float?

Mr. BURKE: I think most of the banks have used them.

Mr. LAMBERT: Yes, but how many major centres in Canada? I think there are three at the present time. I would agree with you this may be true ten years from now, but I am wondering about today.

Mr. BURKE: I am concerned about ten years from now, too, because this would be locked in for ten years and we would find the economic advances

catching up to us to the point where we would be very much behind. The inefficiency of the present method, if you examine how it is done in places of business, and they cannot find any faster way, I have examined many of them, the manpower that is put to work to compute this exchange charge has a very, very serious impact on the wage bill. Then, of course, if these charges are computed, they must be checked. So the bank, I consider, is repeating this process the second time.

Mr. LAMBERT: Yes, I know, but surely to goodness you as a debtor have some responsibility to make sure that you are paying your debt. You are paying it with an instrument in lieu of bank notes and you are also paying it, perhaps, 2,000 miles away by a cheque drawn on your account at some remote point. Is there not a justification for the charge as, for instance, during the Christmas season when ordinary mail takes 5 to 7 days to get across the country and there is a question of float? The person at the other end is getting instant credit for the cheque.

Mr. BURKE: Not until it is deposited.

Mr. LAMBERT: Well, he deposits it, but under the normal circumstances he is able to write a cheque that day or the following day against that item for which the bank has not received any money. It has not gone through the clearing. In other words, it has advanced funds for maybe up to five days. Now, is this not a fair charge?

Mr. BURKE: I do not think it is fair. I think it is so difficult for the average person to compute that in that very point lies the problem.

Mr. LAMBERT: Then how about swinging back to a practice I seem to remember in England during the war. I had to buy my cheque book.

An hon. MEMBER: You still have to buy it.

Mr. LAMBERT: I also now buy my cheque book for a personal chequing account.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well, you have to do that right here in Ottawa?

Mr. LAMBERT: For a personal chequing account, but suppose on a current account, which is what business normally uses, if it were to buy its cheque book and the banks would average their charges on it, would that, shall we say, help things out?

Mr. BURKE: I realize that some function is going on here which costs money, but I do not believe that our present method is a satisfactory way of getting at it.

Mr. LAMBERT: What would you suggest?

Mr. BURKE: I suggest exactly what the royal commission suggests.

Mr. LAMBERT: No charge at all? In other words, that the banks absorb the whole thing; they absorb the costs of float and they absorb the costs of clearing charges?

Mr. BURKE: The royal commission states that there is no appreciable added cost to clearing out of town cheques.



Mr. LAMBERT: Well, I am going to say right here that I differ with the commission on that point. I have not been persuaded by the commission on the material before us, how they came to that conclusion. Thank you, Mr. Chairman.

Mr. WAHN: Well, Mr. Chairman, my questions are similar to those asked by Mr. Lambert. When this question was discussed, as I recall it, with members of the banking association they said that one reason for the charge was to compensate the bank for what I presume is a float that exists. Let me put this question, if I may. If I issue a cheque in Toronto to a payee in Toronto and the payee deposits the cheque in his Toronto bank one day, I presume that my account can be debited the same day or, at any rate, the next day.

Mr. BURKE: I am not aware how fast the—

Mr. WAHN: Suppose I send a cheque from Toronto to Vancouver and the payee receives it in Vancouver: do you believe the cheque will be debited to my account in Toronto on the same day as it would have been had it been delivered to a payee in Toronto, or do you concede there could be some difference in time?

Mr. BURKE: There could be some difference in time but I am wondering with the computer whether or not these occurrences would not—

Mr. WAHN: You feel it may be possible to clear a cheque drawn on a Toronto bank and which is deposited by the payee in Vancouver as quickly as if the cheque had been delivered to a payee in Toronto?

Mr. BURKE: I think there is every possibility of that, sir.

Mr. WAHN: This is just a question of fact which I would think the banks could determine definitely one way or the other. If that is true, then I would agree there is no reason why out of town cheques should bear a clearing charge and in town cheques should not. But if, in fact, it is established that an out of town cheque on the average does take a bit longer to clear and to debit to the payer's account than does an in town cheque, would you not agree that there is an additional interest cost there which someone must bear?

Mr. BURKE: Yes and I think it should be the issuer of the cheque. Under the law that is the proper place.

Mr. WAHN: That is quite true, and you would agree that if the payer sends the payee a cheque which does not carry the proper exchange, legally the payee could send the cheque back and ask the payer to send the cheque in the correct amount? He has that right in law now, but he obviously realizes it is not a very effective right. He does not do it in fact, although he would have the right to it.

Mr. BURKE: That is right.

Mr. WAHN: How are you going to shift that burden? Legally the payer is under that obligation now, but how are you going to make that obligation effective?

Mr. BURKE: Well, that is a very difficult thing to do unless you set up correspondence, unless you—

Mr. WAHN: Does your suggestion not amount to this analysis, that you are not going to make the payer responsible for bearing the cost, you are going to make the banking system bear the cost?

Mr. BURKE: Simply because I believe that in the day of the modern computer that the transfer of this information is possible with just the same speed from major out of town points as it is within town.

Mr. WAHN: Well, suppose there is a time difference. When you clear a cheque in Toronto you are in the same time zone.

Mr. BURKE: That is right.

Mr. WAHN: If you send a cheque to Vancouver it may be deposited in Vancouver at five o'clock Vancouver time, which is eight o'clock Toronto time, and perhaps the bankers have gone home. I do not know. What do you say about this situation?

Mr. BURKE: We have exactly the same problem within our own organization, but electronic devices work at night.

Mr. WAHN: Is this not just a question of fact? Can cheques delivered to out of town points in fact be cleared by electronic computers as quickly as cheques delivered to in town points?

Mr. BURKE: I subscribe to that, yes.

Mr. WAHN: But if that is not so, then there is an additional cost involved despite what the royal commission may have said. The additional cost is not so much in the physical clearing of the cheques but rather in the interest loss. Is that right?

Mr. BURKE: That is correct.

Mr. WAHN: If it is established as a fact—and this can be determined easily, I would think—that there is an additional cost involved, then you agree that you cannot, without a lot of trouble, make the payer bear the cost. He is obligated now to bear the cost but he is not doing it. Your suggestion, then, amounts to the fact that the additional cost, if any, should be borne by the banking system?

Mr. BURKE: Yes, I think so.

Mr. WAHN: Well, that is what I am trying to establish. I think your brief indicates that at the present time the members of your association are bearing the cost to the extent of about \$3 million. That is not a net loss, that just means that the payers are profiting to the extent of the same amount.

Mr. BURKE: The unstated part of that cost, though, is to compute that amount of money.

Mr. WAHN: Well, I can understand that, but knowing the exchange cost I presume the members of your association, being sound business men, consider that a normal cost of doing business under existing circumstances and take that into consideration in the normal mark-up which they make.

Mr. BURKE: Yes, but they are not happy about the wastefulness of it, particularly as they see other countries such as the United States in particular moving into the area of par clearance to the extent that they have done, which is 94.1 per cent.

Mr. WAHN: Well, it would be a question of the banks recovering extra costs, if any, in a more efficient way.

Mr. BURKE: That is right. You will recall that mention was made about buying cheques.

In 1953 it was our association that put before the then finance minister the suggestion that the three cent stamp on cheques up to \$100, and six cents over that, be abolished. That was a very, very time wasting device, and here again people were issuing cheques and omitting to put on the stamp that made it a negotiable instrument. What are you going to do if you receive a cheque from a man for \$200 or \$300? Are you going to write to him at today's cost of a letter which is around \$2.40, and ask him for 6 cents, or ask him for 15 or 25 cents? This is how these things creep in and become very inefficient, I think, in the conduct of business today.

Mr. WAHN: Nevertheless, would you not agree that even under the existing inefficient system, as you have described it, it is really a very inexpensive way that a resident of Toronto, for example, has of paying a debt to a resident of Vancouver. It would be rather expensive if he were to take a plane and go and attend personally and deliver the cash.

Mr. BURKE: That is correct.

The VICE-CHAIRMAN: Plus the amount of the cheque!

Mr. WAHN: I just have one final question. If you agree that a better system could be found, how do you recommend that the bank recover the portion of the cost which it would bear if it assumed the costs involved in bank clearing?

Mr. BURKE: Well, I am not capable of advising the banks how they would go about this, but I am quite sure that they would find ways and means to recover this which would not be as wasteful of manpower as it is today, not only the manpower of their clients but certainly their own manpower internally, because if this is a charge in doing business then someone must verify that it is correctly assessed. So, the computation is done twice.

Mr. WAHN: One suggestion which was made was that the bank would not credit the payee's account in Vancouver until the cheque had actually cleared the Toronto bank. Would you prefer this system?

Mr. BURKE: Well, if the bank could prove that it was not able to transfer the credits electronically, which I believe they can do.

Mr. WAHN: That is all, Mr. Chairman.

The VICE-CHAIRMAN: Thank you, Mr. Wahn.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): One of the advantages in adopting the proposal made by our witness would be that if the banks are not as far into the modern age as they ought to be they would very soon get there. I have observed that Air Canada consumes no more time in getting information about a reservation for me from Vancouver or Edmonton as it does from Toronto or Ottawa. It is almost instantaneous.

Mr. LAMBERT: But how do you know you are not paying for that?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Probably I am, I do not know. I do not think so, though, because actually they have cut down their costs by doing this. They do not have the elaborate performance they used to have, which was a very time wasting and a very expensive cost, and that is why Air



Canada put that in. If the banks have not done so, then I suggest that every move we can make to force them to do this should be taken. However, I suspect they do it.

Mr. CLERMONT: Perhaps they will note the signature on the cheque. It is all right to make a reservation for a seat on a plane, but for a cheque that is signed by somebody in Vancouver to be cashed on an account in Montreal—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The information about that person's account can be transmitted instantaneously, which I presume is what is done.

The VICE-CHAIRMAN: Before asking Mr. Clermont's reaction to this I would just like, if I may, to clarify two points.

Does the bank charge anything regarding the clearance of certified cheques?

Mr. BURKE: That I cannot answer.

Mr. CLERMONT: There is no difference.

Mr. BURKE: I beg your pardon?

Mr. CLERMONT: There is no difference between a certified cheque or an uncertified one. There is a bank charge.

The VICE-CHAIRMAN: And what about the N.S.F. cheques?

Mr. BURKE: I think the banks are imposing a charge.

(*Translation*)

The VICE-CHAIRMAN: Mr. Clermont, please.

Mr. CLERMONT: Mr. Burke, you said the banks would find other means for compensating the loss they claim they would have, but the Porter Royal Commission admits that someone has to pay, because they claim the Federal Government should pay for these cheques, the banks claim they lose \$7 millions in cashing Government cheques. Does that mean the banks should get compensation by going into other fields, that the customer would pay extra?

(*English*)

Mr. BURKE: I do not feel qualified to discuss the government's position on this. They point out in the report that they—

Mr. Clermont: Mr. Burke, I gave the government as an example. The banks claim they are losing \$7 million a year by cashing federal government cheques. If all cheques are cashed without charge that means the banks, according to their claim, will lose more money and somebody will have to pay to recover that supposed loss of money.

Mr. BURKE: I submit, sir, that if exchange was computed on all government cheques and the banks had to check the accuracy of that, it would be very much more costly than they claim it is today.

Mr. CLERMONT: Yes, but you mention in your report that in Europe they do not have the bank charges, but I understand in many countries of Europe they have what they call a transfer of credit?

Mr. BURKE: That is right.

Mr. CLERMONT: Where a customer will go to his bank and ask his bank to transfer so much money to somebody else in another bank and debit his account?

Mr. BURKE: That is right, and I would imagine he has to pay for that privilege.

Mr. CLERMONT: So is there any difference? The bank will get the charge.

Mr. BURKE: Well, in that case the bank is performing a specific clerical task. Under our system the cheques are written and submitted to the banks.

Mr. CLERMONT: I am sure you are aware of clause 92 of Bill No. C-222?

Mr. BURKE: Offhand I am not, no.

Mr. Clermont: If this bill is approved, and comparing it with the chart you have given us, you will pay more money than you pay now, because in some cases it is one-tenth, one-twentieth and one-thirty-second and with Bill No. C-222, clause 92, it is a maximum of one-eighth and a maximum of one-quarter. That is clause 92(a) and (b).

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Perhaps we should delete that, Mr. Clermont.

Mr. CLERMONT: Yes, but I am afraid, Mr. Cameron, that somebody else will have to pay what the banks claim they will lose in money.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I expect so, if they have anything to do with it.

(Translation)

Mr. LATULIPPE: A supplementary question, sir?

The VICE-CHAIRMAN: A moment, please.

(English)

Do you have anything to say with regard to Mr. Cameron's comment or Mr. Clermont's?

Mr. BURKE: There is only one thing I would like to say in connection with that. It says the bank "may". I would certainly like to suggest to this committee that they examine the background information that would cause the royal commission to make the statement it made that there is no significant extra cost involved.

Mr. CLERMONT: Thank you.

The VICE-CHAIRMAN: Thank you, Mr. Clermont.

Mr. CAMERON: You do not have a question?

(Translation)

Mr. LATULIPPE: May I ask a supplementary question to Mr. Clermont's question. I read somewhere in the Porter report that the Government leaves certain reserves to the banks to compensate the expenses for the exchange of cheques. I do not remember where I found it, but I did read it in the report. The banks are allowed certain reserves to compensate for the handling of cheques. Is it not the case?

(English)

Mr. BURKE: This is on page 394, sir, of the Porter report, and it says:

It is true that the banks gain some advantage from government balances maintained with them in the ordinary course of events, although there is no guarantee of this and balance over \$100 million are paid interest at a rate very close to that on treasury bills.

(Translation)

Mr. LATULIPPE: Could you tell us what is the total circulation of cheques, the total value of cheques handled?

(English)

The VICE-CHAIRMAN: Do you have that information, Mr. Burke?

Mr. BURKE: That information is in our brief. To the end of 1964 the total value is \$162,045,990,000. And as you can see that has gone up very appreciably since 1938, when it was \$11 billion.

(Translation)

Mr. LATULIPPE: I saw also somewhere there was a circulation of 520 billion. This does not correspond to the figure you gave us—520 billion.

(English)

Mr. BURKE: My figures are from the Dominion Bureau of Statistics, catalogue 61001 monthly, and when we submitted the brief the latest figures available were for the year 1964, and at that time it was \$162,045,990,000.

(Translation)

Mr. LATULIPPE: The statistics I have seen were for the year 1966, but I cannot remember where I found them, but I seem to remember the figure was 520 billion. However, if we take out \$3 million, it means that the discount charged by the banks is not charged on the whole volume of cheques, because the amount would be far greater than that.

(English)

Mr. BURKE: Unless I have misunderstood you, sir, I thought you asked for the value of the cheques cashed, and that was the figure I gave.

The VICE-CHAIRMAN: No, he asked for the number of cheques.

Mr. BURKE: The number of cheques? I do not have that figure.

Mr. CLERMONT: Mr. Burke, I do not think when you mentioned \$2,900,000 and something it is what the banks are charging, it is only 37 per cent of what your 4,000 members said?

Mr. BURKE: That is right, exactly.

Mr. CLERMONT: Besides that there are many more organizations and other people that are paying bank charges throughout Canada.

Mr. BURKE: That is perfectly correct.

Mr. CLERMONT: I am sure that the bank charges to cash cheques are much more than \$2,900,000.



Mr. BURKE: I was just giving an example of having tested this with our membership to determine—

Mr. CLERMONT: And only 37 per cent of your membership replied?

Mr. BURKE: Yes, and if you will notice it is broken down into the various industries. Take the packinghouse industry, for example, where terms are weekly; in essence they get 52 cheques every year from every one of their customers, so this is a very large job with them in making up their daily deposits.

Mr. LAMBERT: I have a supplementary, Mr. Chairman.

The VICE-CHAIRMAN: Yes, Mr. Lambert.

Mr. LAMBERT: In your tabulation, though, you did not indicate how much each of these firms estimated it saved by not putting exchange on their cheques that they send out to their creditors?

Mr. BURKE: Well, here is where the discrimination bit comes in. They arrange par clearance.

Mr. LAMBERT: Yes, but you know as well as I do how you arrange par clearance. You either keep a sufficient balance or you pay a general fee.

Mr. BURKE: Or you borrow.

Mr. LAMBERT: But you are paying for that.

Mr. BURKE: In other words, you give the bank compensating revenue in other fields.

Mr. LAMBERT: That is so. You are the one who makes the arrangements. All right, that is my supplementary question. However, I have another question to ask. If the banks were to absorb all the costs of cheque clearances this would presumably mean a reduction of their profits. They are taxed at 50 per cent on their profits and the net result of your submission is that the government of Canada is being asked to pay 50 per cent of the costs of doing business by cheque across the country?

Mr. WAHN: We collect 50 per cent on their savings, though.

Mr. BURKE: I again go back to the statement that has been made that there is no significant extra cost to clear out of town cheques.

Mr. LAMBERT: Well, there I part company with the commission.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You parted with them an hour ago, Mr. Lambert.

Mr. LAMBERT: What would your views be about buying all your cheques whether you are an urban customer, a city customer or a general customer, no matter where you were, if you paid a flat charge of 15 cents or 10 cents per cheque and you could only use that particular form of cheque for bank X?

Mr. BURKE: Well, I currently buy my cheques from the bank because my name is imprinted on them and my account number is imprinted on them in magnetic ink.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Also your computer number?

Mr. BURKE: Yes.

Mr. LAMBERT: Well, what would be the views of your members? Perhaps you have not been able to test them on this, but would they be prepared to buy their cheques from the banks on a flat rate even though 75 per cent of their business was done within the one clearing area on which there would be no exchange chargeable?

Mr. BURKE: I could not commit them by answering that question.

Mr. LAMBERT: It would be interesting to know.

Mr. WAHN: I have a supplementary question now in view of what Mr. Burke has said. I believe in answer to Mr. Lambert you said that many of your members were able to arrange par privileges on outgoing cheques and for that reason you did not deduct from your members the cost of bearing the exchange, which was a saving that you might make by not having to pay exchange on the cheques that you issue in payment of your debts. If your members can arrange par clearance for outgoing cheques, can you not also arrange par clearance for incoming cheques? I thought there was something in your memorandum which indicated that that was possible?

Mr. BURKE: No, not to my knowledge.

Mr. WAHN: So, you cannot make arrangements with your bankers whereby the cheques you receive are free of exchange?

Mr. BURKE: No. Some of our customers, however, get the bank to compute the exchange on their cheques and the bank makes a charge for this additional service. I look at the units of money involved here and the clerical time to compute these. I feel that it is—

Mr. LAMBERT: What about having an educational campaign to encourage people to include the exchange when they pay their debts?

Mr. WAHN: I had not quite finished my question. If you will look at page 3 of your memorandum, Mr. Burke, subparagraph 1 of paragraph 11 reads:

Presumably by virtue of the competitive situation among the chartered banks of Canada, certain of their customers are permitted as payer and/or payee to negotiate their cheques at par.

Does not that mean that some of your members can make arrangements with the chartered banks whereby incoming cheques on which they are payees are negotiated at par?

Mr. BURKE: Well, if the payee has negotiated with his bank for par clearance and it is printed right on the cheque. The general phrase is "This cheque is payable at par at all branches across Canada except far northern branches".

Mr. WAHN: That would be where the payer had made those arrangements. Look at this paragraph—

Mr. BURKE: Well, what I think is intended here is if the payee has also made those arrangements there is going to be no charge.

Mr. WAHN: On cheques which are payable to him?

Mr. BURKE: Cheques that he receives which have that notation on them. There is no charge for those. But where there is no notation to the effect that the cheque is payable at par, then the exchange applies.

Mr. WAHN: Thank you, Mr. Chairman.

Mr. CLERMONT: Mr. Burke, most of your claim that there should be no charge is based on the Royal Commission on Banking but, on the other hand, the same commission recommends that the clearing arrangements should be made through the Bank of Canada instead of through the banking association. When the Governor of the Bank of Canada was here as a witness he claimed it was not desirable that clearing arrangements should be made through the Bank of Canada.

Mr. BURKE: There is a footnote at the page of 394 which says:

Even if the central bank were gradually to assume a larger role in the mechanical job of clearing, and we see no advantage in its doing so, we find it hard to believe that this would enable it to pry into the affairs of. . .

And so on. As I read that the commission saw no advantage in the central bank doing it.

The VICE-CHAIRMAN: Have you concluded, Mr. Clermont? Then, as no other members wish to ask questions, Mr. Burke, I thank you very much on behalf of everyone for the interesting points you have raised before us. You can be sure that your suggestions will be taken into consideration by all the members when studying the amendments to the bill.

Mr. BURKE: Thank you, gentlemen.

The VICE-CHAIRMAN: This meeting is now adjourned until a further date in January of next year, which will be decided by the steering committee when they meet tomorrow.



**APPENDIX "AA"**

TO THE STANDING COMMITTEE ON FINANCE,  
TRADE AND ECONOMIC AFFAIRS  
HOUSE OF COMMONS, OTTAWA, CANADA

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**ADDENDUM TO**

A SUBMISSION ON SECTIONS 60 and 63 OF BILL C-222  
(formerly Bill C-102)

AN ACT RESPECTING BANKS AND BANKING

By

R. CATERINA, CARLETON UNIVERSITY, OTTAWA, CANADA

31 October 1966

The objective of this addendum to a previous submission on Bill C-102 is twofold:

- (a) To draw the Committee's attention to the points raised in that submission which are equally applicable to Bill C-222;
- (b) To point out the inadequacies of Schedule P, and of the auditors' report as required by Bill C-222.

#### *Schedule P, Section 60(c)*

The addition of this Schedule will provide shareholders with more information on the financial position and on the performance of the banks than is now available to them. This is a welcome addition, but it falls short of adequate disclosure.

It is generally known that banks appropriate amounts for general undetermined events. These appropriations (commonly known as *reserves for contingencies*) form part of the shareholders equity, and should be stated if a reasonable disclosure of equity capital is to be provided. Schedule P makes no provision for this, and it should be amended to require disclosure of this type of appropriation together with changes in it from period to period.

The title "Transferred to tax-paid appropriations" in Schedule P, would indicate the existence of tax-paid accumulated appropriations (these may well be the reserves for contingencies referred to above) whose amount or transfers from are nowhere disclosed in Schedules N, O, or P. To be consistent with the implied aim of Schedule P, the same information should be disclosed for this item as is proposed for the accumulated appropriations for losses on loans and investments.

In connection with the accumulated appropriations for losses on loans and investments, it should be indicated whether they represent the maximum amount permitted under the Income Tax Act and Regulations.

#### *Auditors' Report to the Shareholders—Section 63(12)*

Section 60(2) (a)(b)(c) of the Bill specifies the reports which the outgoing directors shall submit at every general annual meeting of shareholders. These are:

1. "A statement of assets and liabilities of the Bank as at the end of the financial year, . . . Schedule N." Section 60(2)(a);
2. "A statement of revenue, expenses and undivided profits of the bank for the financial year, . . . Schedule O . . ." Section 60(2)(b);
3. "A statement of the accumulated appropriations for losses on investments and loans of the bank for the financial year, . . . Schedule O . . ." Section 60(2)(c). Section 63(12) states:  
"The auditors shall make a report to the shareholders on the statement of the assets and liabilities and on the statement of revenue, expenses and undivided profits of the bank . . ."

It should be noted that whereas Section 60 requires three schedules to be submitted at the annual general meeting of the shareholders, Section 63(12) requires that the auditors report on only two of them; namely, Schedules N and O. This seems to be an obvious omission in Section 63(12), and should be amended to include Schedule P as well.

Subsection 13 of Section 63 sets forth the content of the auditors' report to the shareholders.

"The auditors' report shall state whether, in their opinion, the statement referred to in the report present fairly the financial position of the bank as at the end of the financial year and its revenue, expenses, and undivided profits for the year...".

Aside from the omission of Schedule P noted above, the content of the auditors' report is deficient in another respect.

It is well known in the accounting profession that different methods may be employed to determine financial position and revenue and expenses, and for this reason the Canadian Institute of Chartered Accountants (Bulletin No. 17) and the Canada Corporations Act (section 124 (2)) require the auditors to state (a) the method used in determining profits and financial position; (b) whether the method used is consistent with that of the previous year. Bill C-222 does not require the auditors to meet these basic requirements.

It is recommended that Section 63(13) be amended to include a statement by the auditors on:

- (a) Method used in determining financial position, revenue and expenses;
- (b) Whether the method used has been applied consistently from period to period.



TO THE COMMITTEE ON FINANCE, TRADE AND ECONOMIC AFFAIRS,  
HOUSE OF COMMONS, OTTAWA, CANADA

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A SUBMISSION ON SECTIONS 60 and 63 OF BILL C-102,  
AN ACT RESPECTING BANKS AND BANKING  
By R. Caterina, Carleton University, Ottawa, Canada

### *Introduction*

Depositors' safety has been the prime goal of banking legislation since its beginnings. This preoccupation, though a real one, has been carried to a point where the interests of the depositors and those of the shareholders have been made to appear incompatible. Partly on account of this view, the rights of chartered banks shareholders have been unduly abridged.

The annual reports of the banks are a clear indication of the extent to which the rights of the shareholders have been limited. In the name of depositors interest and public confidence, the shareholders have been kept substantially uniformed of the management of their affairs. Fears of misunderstanding, panic, and a return of the Depression, have been the main reasons for allowing banks to withhold more significant information than they convey. In 1960, these apprehensions were expressed to the Jenkins Committee on Company Law by the Committee of London Clearing Bankers in its case against more disclosure by banks.

Subscribing to the view that confidence is essentially built on knowledge of the relevant facts; and fully endorsing the right of shareholders to obtain meaningful information, I respectfully submit for your consideration my thoughts on that part of The House of Commons of Canada Bill C-102, An Act respecting Banks and Banking, as it deals with the annual reports of the chartered banks to the shareholders.

### *The present state of chartered banks reporting to the shareholders*

If it be granted that shareholders are entitled to obtain adequate, periodic, information concerning the financial position and operating results of the bank whose shares they own, then, it must be concluded that they have fared poorly.

Generally, shareholders of Canadian chartered banks receive only annual reports, and the information contained therein is inadequate to judge financial position, uninformative to assess operating performance and, to the extent that not all of the facts are shown, misleading.

To be sure, chartered banks have fully complied with the Bank Act in reporting to their shareholders. If their annual reports are inadequate it is because the law, while adequate in the light of the business philosophy and practice prevailing at the time it was written, has been made wanting by the rapid and recent developments in financial reporting in general.

In addition, it is fair to say that on the one hand the managements of the chartered banks have shown a remarkable degree of adaptability to a changing business environment, while on the other hand they have shown little flexibility in adjusting to changes in reporting standards.

Briefly, it can be stated that, from the point of view of financial reporting, the shareholders of the chartered banks are being poorly informed vis-a-vis the shareholders of industrial and commercial corporations, and those of financial corporations other than insurance and trust companies. Yet, the May 1965 issue of the White Bulletin published by the Canadian Bankers Association states that there were in 1964, 99,973 shareholders who owned banks' shares, and 87.3 per cent were Canadian residents.

*The views of the Royal Commission on Banking and Finance*

The philosophy underlying the reporting practices of the chartered banks is stated clearly in the Proceedings of each revision of the Bank Act. Crudely summarized, it amounts to this: the best interest of the depositors, shareholders and the public is best served if they do not know all the significant facts.

This philosophy has denied the shareholders the right to information on which investment decisions are usually based. It is not suggested here that correct decisions are always made when relevant facts are known, but it is suggested that more rational decisions are likely to be made.

As the Report of the Royal Commission on Banking and Finance points out on page 357—

“...no regulatory framework can protect the investor in financial assets from losses if he is determined to speculate or if he does not investigate the financial position or reputation of the institutions with which he plans to deal. Nor can regulation guarantee that there will never be incompetent, negligent, or even dishonest management in the financial system, unless every transaction were to be investigated ahead of time and our economic life brought to a complete halt...”

In our view, the goal of protecting the public against loss can best be achieved with three basic legislative safeguards—adequate disclosure, competent supervision, and legal powers giving the authorities the right to force the correction of unsound or careless practices and to prosecute those engaged in fraudulent or criminal activities. Complete and continuing disclosure of the affairs of institutions should enable the public without unreasonable cost and inconvenience to obtain the necessary information about the reputation and strength of any financial concern, while competent and frequent self-regulation under the ultimate supervision and inspection of government is the best safeguard against an institution becoming insolvent although—of course—not a guarantee that it will not do so.”

*Bill C-102: Its provisions on annual statements and shareholders' audit.*

Sections 60 and 63 of the Bill set out the statutory requirements for the annual financial statements and the auditors' report thereon. Schedule O, Section 60(2) (b), is a welcome, but inadequate, addition, as is the new wording of the auditors' report proposed by section 63(13).

The provisions of these two sections, with related schedules N and O, fall substantially short of the objective assigned to financial reporting by the Royal Commission on Banking and Finance whose views were referred to above. These same views are shared by the business community generally, as is indicated by the quality and increasing frequency of financial news and reports provided; and are heavily relied upon by the banks whenever they process applications for business loans.

I submit that the shareholders of the chartered banks will continue to receive little benefit from the money spent by their management on the preparation of statements of the type provided by schedules N and O, and from the type of statutory audit proposed by section 63.



*Specific Recommendations on Schedule N, Section 60(2) (a)*

Those assets and liabilities which require more adequate and/or meaningful disclosure will be dealt with individually, and in the same order as they are listed in Schedule N. In each case the reason for the recommended change will be stated, and the proposed disclosure indicated.

## ASSETS

*Items 6, 7, 8—Securities Investments*

For commercial banks, liquidity, that is the ability to meet withdrawals without hardship, is more important than profitability. Since investments in securities have ranged between  $\frac{1}{4}$  and  $\frac{1}{2}$  of total assets over the past fifteen years, their maturity dates would convey substantial information on liquidity.

For shareholders, excessive liquidity of the investments portfolio can be as bad as lack of it if liquidity is maintained at the expense of profitability. It is of real interest to them, therefore, to be able to estimate to what extent management is balancing the objective of liquidity with that of profitability.

Information on maturities should be readily available to management, and it could be provided to the shareholders in a manner such as the following:

At the year-end, securities held in the bank's portfolio  
had the following maturities:

	Federal Government % of total held in this category	Provincial Governments % of total held in this category	Other % of total held in this category
Under one year .....	....	....	....
One to two years ....	....	....	....
Two to five years ....	....	....	....
Five to ten years ....	....	....	....
Over ten years .....	....	....	....

*Item 11—Other loans, less provision for estimated loss*

Presumably, this item includes loans made to businesses and personal loans. The report of the General Manager included in the annual report usually makes separate reference to personal and business loans. The relative importance of personal loans has been increasing over the years, and at present they stand at about one half the amount of business loans.

Since the two types of loans, business and personal, are of a different nature and involve different types and amount of risk, and on the liabilities side personal savings deposits are shown separately from business deposits, it would seem logical that personal and business loans be also shown separately on the assets side. Such a presentation would convey a clearer indication of resources allocation and related risks.

*Item 13—Securities of and loans to corporations controlled by the bank.*

The more common methods used by banks to expand their range of services may take the form of:

1. Formation of a new and separate legal entity fully capitalized by the bank.
2. Purchase of an interest in an existing company.
3. Participation in the formation of a new company.

Whatever the method of expansion, the reasons are usually the same: to provide services which may not be provided by the bank as such because of legal restrictions or custom; to commit a portion of the bank's resources to more attractive uses.

The resources committed to these alternative uses are not reasonably accounted for in the statements of the bank itself. The existing Bank Act and Bill C-102 require that for each of the controlled corporations which are not consolidated, individual statements of assets and liabilities, and information on the amount at which the investment in each controlled corporation is carried on the books of the bank, should be provided. But no provision exists in the present Act, or is proposed in Bill C-102, in connection with the accounting, on the books of the bank, for the profits earned by the controlled corporations which are not consolidated.

It is recommended that, in those cases where the statements of the controlled companies are not consolidated with the statements of the bank, subsection 2(a) of section 60 of Bill C-102 be expanded to require some explanation of how, and to what extent, the profits or losses of the controlled corporations which are not consolidated have been taken into account in the books of the bank. This explanation would contribute to a better understanding of the composition of the profits reported by the banks.

*Item 14 of the assets and item 7 of the liabilities—*

*Acceptances guarantees and letters of credit.*

In the normal course of business, banks will undertake certain commitments on behalf of their customers with a view to facilitate their financing.

The commitments the banks make usually take the form of acceptances on behalf of customers, guarantees of various sorts, and the granting of letters of credit. Typically, these services will be offered by the bank only if it feels assured that its customers will provide the required funds in advance of the maturity date of the commitment. Unless the applicant for these services is of high credit standing, a bank will not commit itself.

In effect, then, a bank is only a secondary obligor on these commitments and its liability is only contingent upon the primary debtor's default. At the same time that the bank assumes a contingent liability, it acquires an equal contingent claim against the customer.

Financial statements do not include contingent assets amongst the resources, and contingent liabilities are accorded treatment in the way of an explanatory note. There is no justification for the banks to include contingent assets and contingent liabilities in their balance sheets, except perhaps by footnote. The inclusion in a balance sheet of assets and liabilities which in fact do not exist serves no useful purpose, and the practice should be discontinued.

It is recommended that item 14 of the asset side, and item 7 of the liability side of Schedule N be eliminated, and the provision be made for disclosing contingent liabilities by way of an explanatory note.

The Morgan Guarantee Trust Company of New York, one of the New York banks that has had its 1964 annual statements prepared on a generally accepted basis, has used this approach. Had Canadian chartered banks followed the same approach, the total assets and total liabilities of the system at October 1964, would have been \$671 million lower.

## LIABILITIES

*Items 9, 10, 11—Capital paid up, Rest account, Undivided profits.*

Theoretically, the sum of these account balances should show the equity of the shareholders in the bank. In fact, the provisions of the existing Bank Act and those proposed by Bill C-102 prevent these accounts from conveying the information implied in them.

There are two reasons which make meaningful analysis and understanding of these accounts difficult, if not impossible. The first is the heterogeneous nature of amounts included in the Rest account; the second is the total absence of information on the inner reserves.

### *Rest account*

The heterogeneous nature of the amounts included in this account can best be understood from the analysis which the Bank of Canada Statistical Summary Supplement for 1963 shows on page 34 for the 25 year period 1939-1963, and for 1963 only. The figures relate to the entire banking system.

	1939-63	1963
From operating earnings and undivided profits .	\$ 199.7 million	\$ 20.3 million
From retransfers from inner reserves, net ....	222.7	12.5
From premium on new shares .....	306.2	17.5

It is evident from this analysis that a very substantial portion of the amount accumulated in this account has been paid in by the shareholders, and not earned by the banks. For individual banks, the proportions of each of the three components may be different. A total of, say, \$100 million for each of banks A and B may be made up of \$25 million of retained earnings and \$75 million of paid-in premiums for bank A and vice versa for bank B. In the absence of any additional information, comparative analysis of policies cannot be carried out in an adequate manner, and the reader of the financial statements of banks A and B will likely arrive at the wrong conclusion.

The information on paid-in surplus is evidently available, else the Bank of Canada would not have been able to prepare the analysis for the entire banking system. There is, therefore, no apparent justification for not segregating earned surplus and paid-in surplus on the annual reports to the shareholders.

It is recommended that item 10 on the liabilities section of Schedule N be broken down between the earned and the paid-in portions.



*Inner Reserves*

However well-managed a business may be, it cannot fully avoid the possibility of losses. Management, aware of this problem, copes with it by establishing allowances and/or reserves to cover the losses which may be sustained.

Allowances, or provisions, are established to provide for losses which are normally expected to occur, such as the estimated bad debt losses. Past experience, and current business conditions, are the guiding factors in the determination of the amount which is to be provided for. The amount of the estimated and expected loss for the period is a current cost of doing business, and is applied against current revenues.

Reserves, on the other hand, are appropriations of retained earnings, or profits, made at the discretion of management for any number of reasons, or required by contractual agreements. Reserves are not a current cost of doing business and, accordingly, are not charged to current operations. Reserves for contingencies, for future price declines, for plant expansion, for sinking fund, are examples.

The annual reports of industrial and commercial companies always disclose the amount and type of reserves which may exist, and though it is not mandatory for them to disclose the allowances, a large number do.

Chartered banks, like other businesses, expose themselves to a certain amount of risk, and consequent losses, when they transact business. When they make loans, they expect that not all the amounts may be collected in full; when they buy securities, they are aware that market prices may fluctuate, and they may incur losses if they choose to sell when market prices have fallen below those prevailing at the time of purchase. Loans and securities losses are normal for the banking business and, through experience and expertise, banks appear to be able to control them.

Banks, like other businesses, provide for losses in advance of actual realization. The amount provided is determined on the basis of statutory rules and management's judgement of the business conditions prevailing at the time.

Evidence found in the Bank of Canada statistics, indicates that only a portion of the amounts provided is for estimated and expected current losses. A relatively significant part is in the nature of a reserve, or appropriation, for conceivable but uncertain and undeterminable future price declines of securities; and for conceivable but uncertain, and undeterminable future deterioration of economic conditions which could lead to a deterioration of the loans portfolio.

The allowances and reserves established by the banks are neither segregated nor disclosed in the financial statements. Nor is there any information available on how and to what extent the reserves are used.

If the events for which the reserves are set up do materialize, and unusual losses occur, shareholders would not have any knowledge of these facts. It is not known whether the reserves are being used to absorb normal operating losses or to equalize profits. The amount at which the reserves of each individual bank stand is also unknown.

The prevailing situation is most undesirable. To the extent that very important information is not given, the shareholders are denied the right to assess the performance of their investment and of the banks' managements.

Bill C—102 makes a slight attempt to correct this situation by requiring disclosure of:

- (a) appropriations for losses on loans and investments;
- (b) transfers from accumulated appropriations for losses on loans and investments.

These disclosures, though necessary and welcome, are not sufficient to overcome the problem.

Schedules N and O make no attempt whatsoever to provide information on any of the following questions: On what basis are the annual appropriations made? Are they made on the basis of maximum current tax benefits, or are they made on the basis of prevailing operating conditions? Are the annual appropriations, however determined, consistent with the losses on loans and securities which banks experience? At what amount do the accumulated appropriations stand, and what changes occur in them?

It is respectfully submitted that information pertaining to these legitimate questions can be provided in the annual statements without detrimental effect to the depositors and the public. A large number of U.S. banks follow this practice, and evidence of this is provided on the following page, and in the appendix. First National City Bank, New York, 1964 annual report, page 30.

RESERVES

The Reserve for Possible Losses on loans is a statutory reserve, the maximum amount of which is governed by Treasury Department regulations. Recognized loan losses are charged to this reserve and subsequent recoveries are added. This reserve has been deducted from Loans in the Consolidated Statement of Condition.

Profits or losses from sales of securities, after tax effect, and other non-operating items are added to or deducted from the Reserve for Contingencies. In the Consolidated Statement of Condition, this reserve appears separately with the liabilities.

The total of the Reserve for Possible Losses on loans and the Reserve for Contingencies is \$259,247,000 at December 31, 1964 compared with \$229,219,000 at the prior year-end. Changes in both reserves in 1964 are show in the table below.

Changes in Consolidated Reserves	Reserve for Possible Losses (on Loans)	Reserve for Contingencies
Balance at December 31, 1963 .....	\$ 143,134,000	\$ 86,185,000
Additions:		
From Undivided Profits .....	7,467,000	16,285,000
Tax Benefit Related to Transfers from Undivided Profits .....	7,933,000	—
Other Additions .....	—	1,593,000
	<hr/>	<hr/>
	\$ 158,434,000	\$ 104,063,000
	<hr/>	<hr/>

## Deductions:

Charge-offs, Net Recoveries .....	\$ (520,000)	\$ 2,432,000
Losses from Sales of Securities, after Tax		
Effect .....	—	979,000
Other Deductions .....	—	359,000
	<hr/>	<hr/>
	\$ (520,000)	\$ 3,770,000
	<hr/>	<hr/>
Balance at December 31, 1964 .....	\$ 158,954,000	\$ 100,293,000
	<hr/>	<hr/>

Another forceful example of current thinking on financial reporting by banks is afforded by a report of the New York *Times* Service published in the June 30, 1965 issue of the *Globe and Mail*.

While in the process of offering a capital notes issue of \$266,307,500, the First National City Bank of New York learned that one of its foreign branches had incurred an after-tax loss of \$4,000,000 on foreign exchange transactions.

"Because the First National City Bank was in the midst of a huge offering of capital notes, its management was faced with the problem of whether to disclose the loss.

According to Bernard T. Scott, controller of the Bank, First National City's lawyers concluded disclosure was not necessary because the size of the loss was not significant in relation to the size of the bank (Assets of about \$13.2 billion; operating income of about \$½ billion).

The bank has a reserve for contingencies, now amounting to about \$106,000,000, but a decision to charge off the foreign exchange loss against this reserve would run counter to the recent trends in approved accounting practice. This seeks to make the statement of current income as informative and realistic as possible.

Because the loss would show up in the June 30 earnings statement, the bank's management decided to make the disclosure in its June 10 circular in fairness to investors in the notes."

The examples reproduced show that Schedule O of the Bill will not shed adequate light on the operating performance of the banks. The quotation from the *Globe and Mail* indicates clearly the importance of disclosing changes in reserve accounts to assure the investor that operating losses are charged against current revenues, and that reserves are used only for the purposes for which they are established.

It is reported in American literature that about a century ago Montreal bankers were invited to the United States to explain to their American counterparts the accounting and reporting problems of banking operations. It would be very helpful to us now if Canadian bankers gave serious consideration to the best of current reporting practices by U.S. banks.

It is recommended that Schedules N and O of the Bill include a provision requiring disclosure of the amount and purpose of each reserve, and of the changes which occur in each reserve from period to period.



### *Shareholders' Audit*

It was stated on page 4 that the shareholders will receive little benefit from the statutory audit proposed by Section 63. The reasons underlying this position will now be explored.

Sections 63(12) and 63(13) state:

63(12) The auditors shall make a report to the shareholders on the statement of revenue, expenses and undivided profits of the bank to be submitted by the directors to the shareholders under section 60."

63(13) "The auditors' report shall state whether, in their opinion, the statements referred to in the report present fairly the financial position of the bank as at the end of the financial year and its revenue, expenses and undivided profits for the year, and shall include such remarks as they consider necessary in any case where:

- (a) they have not obtained all the information and explanations they have required; or
- (b) the statements referred to in their report are not as shown by the books of the bank."

Two problems limit the general usefulness of the shareholders' audit proposed by the Bill.

1. Schedules N and O do not require disclosure of and accounting for changes in the inner reserves. The tax free portion was estimated, in a submission to the Porter Commission, at about \$400 million for the entire banking system. If the reserves of each individual bank are not shown anywhere, one would question the validity of the opinion that the statements present fairly the financial position of the bank at the end of the financial year.

In fairness, the opinion should specifically except the reserves if these are not reasonably accounted for or disclosed in the statement.

2. The absence of any indication of the method used in determining expenses and revenues reduces greatly the significance of the profit figure for the period. There is not justifiable reason for omitting this information, and there is little apparent justification for not using generally accepted accounting principles in the determination of profit for the period.

### *Concluding remarks*

The banking industry is not an infant or adolescent that requires excessive protection. It is a mature and responsible industry. It has shown adaptability to changing economic conditions, and willingness to engage in new types of activities. The government virtually underwrites its solvency.

The degree of general and financial literacy prevailing today has dispelled any thoughts of keeping money in a shoe box for fear that banks might close their doors. Witness to this is the growing volume of personal savings deposits and personal loans.

The depression and ignorance psychosis underlying banks' financial reporting is unjustified, and is contradicted by the banks themselves in their search for new and riskier outlets.

The recommendations made in this submission aim at giving shareholders a fair deal. As an alternative or addition to them, I strongly recommend that this

Committee take into consideration the possibility of submitting the financial reports of banks to an impartial review by a Court to determine whether they are reasonable and fair in the light of prevailing circumstances.

If, in the past, limited disclosure was desirable to maintain public confidence, it can only be said that today, inadequate disclosure can only serve to dispel public confidence, and to encourage a lack of faith in banking reports of financial status and operating results.

## Appendix

An example of full disclosure of operating results, changes in reserves, and changes in capital accounts.

## THE FIRST NATIONAL BANK OF CHICAGO

## ANNUAL REPORT 1964

## OPERATING INCOME AND EXPENSES

Operating income was the highest in the bank's history. The increase in interest expense, primarily on our rapidly growing savings and time deposits, was the major expense item, largely offsetting the increase in operating income. Savings and time deposits constituted 43 per cent of the bank's total deposits at the year-end.

## Statement of Operating Earnings

	1964	1963
Operating Income:		
Interest on Loans .....	\$ 102,693,000	\$ 94,445,000
Interest and Dividends on Securities .....	35,383,000	33,414,000
Other Income .....	19,537,000	17,562,000
	<u>\$ 157,613,000</u>	<u>\$ 145,421,000</u>
Operating Expenses:		
Interest .....	\$ 55,940,000	\$ 47,210,000
Salaries, Pension Fund, Profit Sharing, etc. .	27,125,000	26,598,000
Provision for Taxes and Assessments:		
Local Taxes .....	1,350,000	1,350,000
Social Security Taxes .....	632,000	688,000
Federal Deposit Insurance .....	986,000	986,000
Other Operating Expenses .....	13,626,000	12,820,000
	<u>\$ 99,659,000</u>	<u>\$ 89,652,000</u>
Net Operating Earnings (before income taxes).\$	57,954,000	\$ 55,769,000
Less: Federal Income Taxes .....	22,348,000	23,910,000
Net Operating Earnings .....	<u>\$ 35,606,000</u>	<u>\$ 31,859,000</u>
Per Shares .....	\$4.07	\$3.64*

\*On 8,750,000 shares adjusted for a 16 $\frac{2}{3}$  per cent stock dividend paid in 1964.

Operating income in 1964 totaled \$157,613,000, increasing \$12,192,000, or 8.4 per cent, during the year. Interest on loans increased \$8,248,000 as the result of a larger loan volume and slightly improved rates. Interest and dividends on securities rose \$1,969,000. Other income increased \$1,975,000.

Operating expenses amounted to \$99,659,000, an increase of \$10,007,000, or 11.2 per cent, during the year. Again this year, interest expense on a larger volume of time and savings deposits, certificates of deposit and short-term



borrowings added substantially to the operating expenses of the bank. The total interest paid in 1964 amounted to \$55,940,000, compared with \$47,210,000 in 1963, an increase of \$8,730,000. Much smaller increases occurred in other categories of operating expenses.

Net operating earnings (before income taxes) for 1964 totaled \$57,954,000, an increase of \$2,185,000. Federal income taxes on the bank's net operating earnings amounted to \$22,348,000, compared with \$23,910,000 for 1963. Net operating earnings (after income taxes) for 1964 totaled \$35,606,000, an increase of \$3,747,000, or 11.8 per cent, from the \$31,859,000 earned in 1963.

As in previous years, all known losses have been charged off. Following our customary practice, the recoveries during the past year on charged-off items have not been taken into the income account presented herewith, but have been used, together with other additions, to build up the reserves of the bank against future losses.

CHANGES IN LOAN RESERVES

During 1964, net additions of \$18,679,000 increased the loan reserves of the bank to \$76,234,000, which are applied against Loans and Discounts shown on the Statement of Condition.

Summary of Changes in Loan Reserves	
Balance—January 1, 1964 .....	\$57,555,000
Additions:	
Transfers from Undivided Profits .....	6,313,000
Recoveries and miscellaneous credits .....	4,238,000
Other additions .....	8,525,000
Total Additions .....	<u>\$19,076,000</u>
Deductions:	
Loans charged off during 1964 .....	<u>\$ 397,000</u>
Balance—December 31, 1964 .....	<u><u>\$76,234,000</u></u>

CHANGES IN RESERVES FOR SECURITIES

Reserves for securities are applied against the related assets shown on the Statement of Condition.

Summary of Changes in Reserves for Securities	
Balance—January 1, 1964 .....	\$42,211,000
Additions—Net .....	6,483,000
Balance—December 31, 1964 .....	<u><u>\$48,694,000</u></u>

CHANGES IN CAPITAL ACCOUNTS

Certain securities in our investment portfolio were sold during the year, and reinvestments were selected to improve the bank's over-all investment position and its future earnings. Sales of securities and other minor assets resulted in a net loss, after tax adjustments, of \$577,000, compared with a net

profit of \$2,031,000 in 1963. As indicated in the summary of changes in capital accounts, transfers of \$6,313,000 were made to loan reserves.

### Summary of Changes in Capital Accounts

	1964	1963
Balance—Beginning of Year .....	\$ 360,211,000	\$ 338,431,000
Additions:		
Net Operating Earnings .....	\$ 35,606,000	\$ 31,859,000
Investment Security Profits, after Taxes .....	—	2,031,000
Tax Adjustments on Addition to Reserve for		
Bad Debts .....	110,000	3,285,000
Transfers from Other Reserves—Net .....	51,000	2,918,000
Total Additions .....	\$ 35,767,000	\$ 40,093,000
Deductions:		
Cash Dividends Declared .....	\$ 14,000,000	\$ 12,000,000
Investment Security Losses, after Taxes .....	577,000	—
Transfers to Loan Reserves .....	6,313,000	6,313,000
Total Deductions .....	\$ 20,890,000	\$ 18,313,000
Balance—End of Year .....	\$ 375,088,000	\$ 360,211,000

### CAPITAL ACCOUNTS

#### Composition of Capital Accounts (As of the Year-End)

	1964	1963
Common Stock—\$20 Par		
8,750,000 shares .....	\$ 175,000,000	\$ 150,000,000
7,500,000 shares .....		175,000,000
Surplus .....	185,000,000	35,211,000
Undivided Profits .....	15,088,000	
Capital Accounts .....	\$ 375,088,000	\$ 360,211,000

## UNIVERSITY OF TORONTO

Department Of Political Economy  
100 St. George Street  
Toronto 5

January 25, 1966

Mr. Antonio Plouffe,  
Chief of Branch,  
Committees and Private Legislation Branch,  
House of Commons,  
Ottawa, Ontario

*Re: Sections 60 and 63 of Bill C-102, An  
Act Respecting Banks and Banking.*

Dear Mr. Plouffe:

Some time ago I had an opportunity to read a copy of a submission by Professor Caterina of Carleton University on these proposed sections of the new Act. While I did not consult with him in the preparation of his brief, nor in the writing of this letter, I would like to offer my strong personal support for the recommendations he has made.

The argument is untenable that the chartered banks are still entitled to a separate standard of financial disclosure; far from sustaining public confidence in the banking system, this arrangement must undermine it. I think it is fair to say that the state of financial disclosure by banks in this country is so bad that it is accepted by financial analysts with complete cynicism, and the banks' financial statements are just not taken seriously either by them or by any other informed person.

In particular, I would like to urge that financial disclosure by banks cannot be either complete or "fair" without drawing a clear distinction between "reserves" and "allowances", without publication of an analysis of changes in all reserves (including opening and closing balances), and without publication of the banks' share of profit or losses of subsidiary companies controlled by them.

I submit that it is unreasonable to require the use of the word "fairly" in the expression of the auditor's opinion (section 63(13) of the Act). As matters stand the shareholders' auditor should not be required to do more than to acknowledge that in his opinion the financial statements are in conformity with the requirements of the Bank Act. Needless to say, the proper solution is to revise the disclosure requirements of the Act.

These changes could not prejudice any bank in its competition with other banks (subject themselves to the same requirements) and could not undermine public confidence in a bank *that is being managed properly*. I think that if we seriously wish for the survival of an economic system that approximates the one we have today, it is essential that the basic institutions continue to command public respect and confidence. Any arrangement that maintains a position of immunity from public criticism (implied in a failure to insist upon adequate disclosure requirements) cannot be conducive to that end.

I offer these views as my own. I hope that they will draw attention to the importance of Professor Caterina's able (and restrained) submission.

Yours truly,  
J. E. Smyth,  
Professor of Commerce.



## APPENDIX "BB"

## THE CANADIAN CREDIT MEN'S ASSOCIATION LIMITED

Toronto 17, Ontario

October 21, 1966

To the Chairman and Members of the Committee on Finance,  
Trade and Economic Affairs

Gentlemen:

On behalf of this Association we re-submit our brief in support of the Report of the Royal Commission on Banking and Finance respecting "Par Clearance of Out-of-Town Cheques". Originally this was submitted to the Chairman of the Senate Committee on Banking and Commerce and to The Honourable Walter L. Gordon, P.C., M.P., then Minister of Finance and Receiver General of Canada. Later, our brief was re-submitted to The Honourable Mitchell William Sharp, P.C., B.A., Minister of Finance.

We append photostatic copies of page 393 and 394 of the Report of the Royal Commission on Banking and Finance, where it is clearly set out that this "Royal Commission recommends that there be a statutory prohibition on charges for the negotiation of out-of-town cheques". They go on to say that the actual handling does not involve any significant extra cost to the Institutions concerned.

Unless such prohibition is introduced into the new Bank Act we consider that it will remain as it has been in the past—discriminatory.

The Royal Commission in quoting the system in use in many European countries, points out that under that system the recipient gets the full payment owing to him. This, as stated in our brief, is seldom the case in Canada.

Apart from the significant sum of money paid in exchange as set out in schedule "A" of the brief, based on information contributed by 1,302 of our members, which is but a small segment of the total of Canadian business affected, of equal or greater importance is the clerical time involved in determining the proper amount of exchange to be either added to the cheque when drawing it, or deducted from the cheque that does not include exchange when cashing it, and we can conceive of no method that will replace the individual scrutiny of every out-of-town cheque.

It is obvious that our existing method is highly inefficient and above all encourages contravention of the intent of the law wherein the responsibility for full payment of the debt rests with the payer.

It is our sincere conviction that the abolition of exchange on out-of-town cheques and the provision that all cheques be payable at par would serve the following purposes:

1. Remove the present discriminatory practices
2. Provide cheque recipients with full payment
3. Prove of benefit to the entire business community in the elimination of unproductive and unnecessary man hours.

May we, therefore, urge the Committee to ensure that the recommendation included in the report of the Royal Commission on Banking and Finance "that there be a statutory prohibition on charges for the negotiation of out-of-town cheques" form a necessary part of Bill C-222 an Act respecting Banks and Banking.

Respectfully submitted,

A. L. Irwin,  
National President.

THE CANADIAN CREDIT MEN'S ASSOCIATION LIMITED  
6 CRESCENT ROAD  
TORONTO 5, ONTARIO  
CANADA

SUBMISSION OF BRIEF  
to  
THE MINISTER OF FINANCE AND RECEIVER GENERAL OF CANADA  
on  
PAR CLEARANCE OF OUT-OF-TOWN CHEQUES

Presented on behalf of CCMA by:

George Wishart, MCI, FCIS  
National President



# THE CANADIAN CREDIT MEN'S ASSOCIATION BRIEF TO THE MINISTER OF FINANCE AND RECEIVER GENERAL OF CANADA ON PAR CLEARANCE OF OUT-OF-TOWN CHEQUES

1. This Association, in behalf of its 4,000 member companies throughout Canada, urges implementation of the recommendation contained in the Report of the Royal Commission on Banking and Finance, respecting 'par clearance of out-of-town cheques'. (See pages 393-4 thereof.)

2. The responsibility under law is quite clear that the payer, on issuing a cheque, is responsible to ensure that the payee shall receive the full amount owing.

3. Notwithstanding, present practice frequently demands that the recipient of a cheque from an out-of-town source either, (a) accepts payment of a lesser amount—unless the payer has pre-arranged par clearance through his bank—or, (b) endeavours to secure such additional funds from the payer as will reimburse him for the exchange charges applicable.

4. Illustrative of the current exchange charges levied is the following schedule of rates established by one of the chartered banks in Canada.

## *Branch Point*

Cheques Up To \$2500.00	1/8 of 1%	Min. 15¢
Over \$2500. To \$5000.00	1/10 of 1%	Min. \$3.15
Over \$5000. To \$25000.00	1/16 of 1%	Min. \$5.00
Over \$25000. To \$100,000.	1/32 of 1%	Min. \$15.65

Over \$100,000 at the discretion of Manager but minimum must be \$31.25

## *No Branch of the Chartered Bank*

Cheques Up To \$2500.00	1/4 of 1%	Min. 25¢.
Over \$2500. to \$5000.00	3/16 of 1%	Min. \$6.25.
Over \$4000. to \$25000.00	1/8 of 1%	Min. \$9.38

Over \$25,000 to \$100,000—Subject to negotiation or at Manager's discretion but minimum must be \$31.25

## *Exceptions:*

1. Outside of Metropolitan Toronto if there is a branch of the Chartered Bank but no branch of the bank on which the cheque being deposited was drawn the following applies:

5¢ per cheque—Plus 1/10 of 1 per cent of value of cheque being deposited up to \$5,000.00.

Over \$5,000 to \$25,000 1/20 of 1 per cent—Minimum \$5.00 per each item.

Over \$25,000.00—Subject to negotiation—but a minimum of \$12.50 each.

2. Cheques drawn on far northern points—i.e. Fort Churchill would have to check with the bank.

3. Cheques drawn on Caisse Populaire—Rates very similar to Exception 1.

5. From the foregoing it will be apparent that the payer, in order to ensure full payment to the recipient must, when drawing a cheque, ascertain whether there is a branch of his own bank, as well as of the recipient, domiciled in the municipality where payment is to be made, before the express amount of exchange may be determined.

6. The prevailing practice, however, is for the payer to ignore the exchange charges applicable to the amount of indebtedness, by merely drawing the cheque for the net amount. This presents the recipient with the alternative of challenging the omission of the exchange charges applicable, or of accepting settlement of a lesser amount than is due.

7. We submit this is an unfair transfer of responsibility by the payer, to the payee, in contravention of the intent of the law wherein the responsibility for full payment rests with the payer.

8. The survey of its members conducted by this Association indicates that liability for payment of exchange on out-of-town cheques is frequently assumed—not by the payer, but by the payee. In effect, the latter accepts payment of an amount less than the face value of the cheque.

9. The analysis of survey replies, shown in Schedule "A" and forming a part of this Brief, is evidence of the extent of the penalty being exacted against recipients of such out-of-town cheque. Of 1302 respondents representing 33.7 per cent of the Association membership throughout Canada, liability for payment of exchange on such cheques was accepted by them during a twelve-month period, to an amount totalling \$2,940,070.

10. It is apparent to this Association, therefore, that the cost of exchange is unfairly apportioned and is in fact often borne by the payee.

11. Certain observations may be made respecting the current situation of exchange charges and payments:

1. Presumably by virtue of the competitive situation among the chartered banks of Canada, certain of their customers are permitted as payer and/or payee to negotiate their cheques at par.
2. Discretionary powers to negotiate such arrangements with customers suggest the possibility of discriminatory treatment of individual customers.
3. As a consequence of non-inclusion of the exchange involved, recipients of out-of-town cheques not negotiable at par are subject to inequities in the amounts paid to them.
4. Those customers of chartered banks with few branches are placed at a disadvantage, unless such par clearance arrangements have been negotiated.

12. Relevant to the magnitude of the total value of current exchange charges, the likelihood of a steady increase in the future, reference is made to the table shown in Schedule "B", of 'Cheques Cashed in Clearing Centres', published by the Dominion Bureau of Statistics, which clearly shows the continuing trend of expansion in the volume of cheque transactions.

13. Coincident with this examination of the 'direct' costs through loss of exchange receipts by the payer, are the less obvious, yet equally significant 'hidden' costs involved in:

- (a) the preparation of cheques by the payer and the investigation necessary to calculate the appropriate exchange amount,
- (b) the examination by the recipient of the cheque respecting the inclusion, or otherwise of the amount of exchange applicable,
- (c) advance negotiations by the payer, respecting cheque clearance at par,
- (d) subsequent negotiations by the payee respecting possible arrangements of exchange handling, or,
- (e) such other action as the payee may deem necessary or desirable respecting the collection from the payer of the amount of exchange charges involved.

14. It is the opinion of this Association that implementation of the aforementioned recommendation by the Royal Commission on Banking and Finance would resolve or eliminate the costly problems attendant upon the administration of payment of exchange on out-of-town cheques. Such action would:

- 1. re-establish responsibility for full payment of the face value of such cheques, with the payer, in favour of the payee,
- 2. remove any possible inequities in the assessment of exchange amounts payable,
- 3. eliminate the clerical costs involved in this aspect of cheque handling, both for the institutions concerned and for business enterprises throughout the Canadian commercial community.

15. In consequence, this Association vigorously supports the aforementioned recommendation and urges, with all the emphasis at its disposal, its adoption and enactment into the legal statutes of Canada.



## SCHEDULE "A"

ANALYSIS OF MEMBERS REPORTING EXCHANGE TO  
NEGOTIATE OUT-OF-TOWN CHEQUES DOLLAR VALUE

Members Reporting	Industry Classification	Amount Paid
130	Food Products .....	\$ 245,875
8	Footwear .....	24,511
14	Dry Goods .....	47,076
7	Men's & Boys Clothing & Furnishings .....	38,812
22	Marine—Builders Hardware .....	54,033
13	Banking—Finance .....	87,522
16	Mover—Transport .....	47,560
7	Musical Instruments—Records—Sheet Music .....	5,348
7	Paper Products .....	15,121
5	Broker .....	17,408
12	China—Giftware—Novelties .....	9,112
31	Drug—Cosmetic Supplies .....	105,407
17	Flour—Feed .....	94,064
11	Fruit & Produce .....	46,010
33	Furniture—Furnishings—Floor Coverings .....	34,905
17	Photographic Equipment & Supplies .....	16,116
15	Textiles—Knit Goods .....	32,489
30	Construction Machinery & Supplies .....	67,034
24	Jewellery—Diamonds .....	17,551
2	Ladies & Girls' Clothing & Furnishings .....	232
22	Logging—Lumber .....	49,031
9	Agricultural Equipment & Supplies .....	9,460
62	Appliances—TV—Radio—Stereo .....	132,208
20	Meat Packing .....	156,881
58	Industrial & Mining Machinery & Supplies .....	34,959
50	Electrical Equipment & Supplies .....	47,904
18	Advertising Media .....	13,204
19	Petroleum Products .....	301,389
25	Paint—Varnish & Supplies .....	38,996
15	Tires—Rubber Goods .....	30,474
15	Sporting Goods—Playthings .....	12,195
2	Soaps—Detergents .....	1,020
4	Packaging Equipment & Supplies .....	11,401
21	Office Equipment & Supplies—Stationers .....	34,186
25	Plumbing Equipment & Supplies .....	83,844
56	Steel—Metal .....	80,547
35	Heating—Air Conditioning Equipment & Supplies .....	44,614
6	Tea—Coffe—Spices—Flavourings .....	8,685
15	Tobacco—Beverage—Confectioners .....	34,247
101	Multiple Lines .....	215,844
1	Growers—Florists .....	101
1	Dairy Equipment & Supplies .....	1,408
18	Electronic Equipment & Supplies .....	15,054

8	Commercial Fixtures—Furnishings—Refrigeration .....	\$ 2,329
23	Printing—Publishing .....	65,047
89	Automotive Equipment & Supplies .....	105,861
98	Building Materials—Contractor .....	113,234
15	Chemicals—Plastics .....	15,692
50	Classification not specified .....	274,069
1302	Grand Total .....	\$ 2,940,070

## SCHEDULE "B"

Extract from:  
 Catalogue No. 61-001 Monthly,  
 Vol. 41, No. 5, July 1964,  
 as published by  
 Dominion Bureau of Statistics.

TABLE 2

CHEQUES CASHED IN 35 CLEARING CENTRES, DURING THE FIRST FIVE MONTHS,  
 REPRESENTATIVE YEARS

Year	Canada	Atlantic Provinces	Quebec	Ontario	Prairie Provinces	British Columbia
thousands of dollars						
1929.....	19,255,760 <sup>(1)</sup>	324,976	6,694,400	7,987,367	2,956,913	1,292,104
1938.....	11,854,490	250,817	3,789,441	5,547,378	1,527,437 <sup>(2)</sup>	739,417
1943.....	21,117,778	505,842	6,022,708	10,088,089 <sup>(3)</sup>	3,199,371	1,801,768
1949.....	33,954,060	822,513 <sup>(4)</sup>	9,729,592	14,217,479	6,144,781	3,039,695
1950.....	36,469,576	953,471	10,743,830	15,574,074 <sup>(5)</sup>	6,083,703	3,114,498
1951.....	44,315,778	1,151,824	13,144,740	18,932,092	7,137,647	3,949,475
1952.....	49,150,053	1,202,021	14,218,149	20,762,212	8,412,154	4,555,517
1953.....	55,588,130	1,324,811	15,417,018	24,830,805	9,558,672	4,456,824
1954.....	58,409,362	1,368,044	16,828,264	26,226,604	9,192,116	4,794,334
1955.....	62,450,857	1,351,954	18,390,247	28,503,224	9,344,705	4,860,727
1956.....	76,134,648	1,607,754	23,012,928	34,079,542	11,525,829	5,908,595
1957.....	83,798,141	1,672,420	24,873,207	37,909,293	12,833,421	6,509,800
1958.....	85,961,700	1,689,516	25,006,637	39,787,117	13,131,016	6,347,414
1959.....	97,795,119	2,017,714	27,691,098	46,850,343	14,373,315	6,862,649
1960.....	108,659,710	2,191,534	32,187,836	51,781,571	15,310,045	7,188,724
1961.....	115,721,357	2,276,604	34,922,371	53,222,884	17,780,740	7,518,758
1962.....	126,665,359	2,540,670	37,737,743	58,667,062	18,713,550	9,006,334
1963.....	144,120,082	2,997,688	43,811,970	65,738,493	21,934,251	9,737,680
1964.....	162,045,990	3,378,761	49,303,950	74,843,414	23,508,513	11,011,352

<sup>(1)</sup>Original 33 centres.

<sup>(2)</sup>Weyburn data excluded as of 1931.

<sup>(3)</sup>St. Catharines data added as of May 1941.

<sup>(4)</sup>St. John's Newfoundland, data as of April 1949.

<sup>(5)</sup>Cornwall data as of May 1950.

OFFICIAL REPORT OF MINUTES  
OF  
PROCEEDINGS AND EVIDENCE

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Translated by the General Bureau for Translation, Secretary of State.

LÉON-J. RAYMOND,  
*The Clerk of the House.*



HOUSE OF COMMONS  
First Session—Twenty-seventh Parliament  
1966

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STANDING COMMITTEE  
ON  
**FINANCE, TRADE AND ECONOMIC AFFAIRS**  
*Chairman: Mr. HERB GRAY*

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MINUTES OF PROCEEDINGS AND EVIDENCE  
No. 32

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THURSDAY, DECEMBER 15, 1966

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Respecting

Bill C-190, An Act to amend the Bank of Canada Act.  
Bill C-222, An Act respecting Banks and Banking.  
Bill C-223, An Act respecting Savings Banks in the Province of Quebec.

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WITNESSES:

E. P. Neufeld, Professor of Economics, University of Toronto;  
Jacob S. Ziegel, Professor of Law, McGill University.

ROGER DUHAMEL, F.R.S.C.  
QUEEN'S PRINTER AND CONTROLLER OF STATIONERY  
OTTAWA, 1966

STANDING COMMITTEE  
ON  
FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. Herb Gray

*Vice-Chairman:* Mr. Ovide Laflamme

and Messrs.

Addison,	Comtois,	Leboe,
Basford,	Flemming,	Lind,
Cameron ( <i>Nanaimo-</i>	Fulton,	McLean ( <i>Charlotte</i> ),
<i>Cowichan-The Islands</i> ),	Gilbert,	Monteith,
Cashin,	Irvine,	More ( <i>Regina City</i> ),
Chrétien,	Lambert,	Munro,
Clermont,	Lamontagne,	Valade,
Coates,	Latulippe,	Wahn—(25).

Dorothy F. Ballantine,  
*Clerk of the Committee.*

## MINUTES OF PROCEEDINGS

THURSDAY, December 15, 1966.

(63)

The Standing Committee on Finance, Trade and Economic Affairs met at 11:10 a.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Cameron (*Nanaimo-Cowichan-The Islands*), Chrétien, Clermont, Fulton, Gilbert, Gray, Laflamme, Lambert, Leboe, Latulippe, Lind, McLean (*Charlotte*), Monteith, More (*Regina City*), Wahn—(15).

*In attendance:* Messrs. E. P. Neufeld, Professor of Economics, University of Toronto; C. F. Elderkin, Inspector General of Banks; Denis Baribeau and Miss M. R. Prentis, research assistants.

The Committee resumed consideration of the banking legislation.

The Chairman introduced the witness, Mr. Neufeld, who summarized his brief. In accordance with the resolution passed at the meeting of October 13, 1966, the brief is attached. (*See Appendix Y.*)

The witness was questioned on his brief.

The questioning continuing, at 1:05 p.m. the Committee adjourned until 3:45 p.m. this day.

## AFTERNOON SITTING

(64)

The Committee resumed at 3:55 p.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Addison, Cameron (*Nanaimo-Cowichan-The Islands*), Clermont, Comtois, Flemming, Fulton, Gilbert, Gray, Laflamme, Lambert, Latulippe, Leboe, Monteith, More (*Regina City*)—(14).

*In attendance:* The same as at the morning sitting.

Questioning of the witness, Mr. Neufeld, was continued and concluded.

On behalf of the Committee, the Chairman thanked the witness, who was permitted to retire.

At 5:55 p.m. the Committee adjourned until 8:00 p.m. this day.



## EVENING SITTING

(65)

The Committee resumed at 8:20 p.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Cameron (*Nanaimo-Cowichan-The Islands*), Gilbert, Gray, Lambert, Latulippe, Leboe, More (*Regina City*).

*In attendance:* Jacob S. Ziegel, Professor of Law, McGill University; Mr. Elderkin and Miss Prentis.

The Chairman introduced the witness, Mr. Ziegel, who summarized his brief. In accordance with resolution passed at the meeting of October 13, 1966, the brief is attached. (*See Appendix Z.*)

The witness was questioned.

The questioning having been concluded, the Chairman thanked the witness who was then permitted to retire.

At 10.25 p.m. the Committee adjourned until 11:00 a.m. Tuesday, December 20, 1966.

Dorothy F. Ballantine,  
*Clerk of the Committee.*

## EVIDENCE

*(Recorded by Electronic Apparatus)*

● (11.00 a.m.)

THURSDAY, December 15, 1966

The CHAIRMAN: I now call the meeting to order. Our order of business this morning is to hear from our witness Professor E. P. Neufeld, who received his honours bachelor degree in arts from the University of Saskatchewan; his doctorate from the London School of Economics. He spent two years working with the Bank of England and for the past several years has been Professor of Economics at the University of Toronto. I will now call upon Professor E. P. Neufeld to present his brief to us. I have explained to him that we have already had his brief under study for some days and it will only be necessary for him to summarize or extrapolate, whichever he prefers, on the points he raised. Following which we will proceed to deal with the topics contained in his brief.

Professor E. P. NEUFELD (*Professor Economics, University of Toronto*): Thank you very much indeed, Mr. Chairman. I think that it must be said straight away that in my view Bill No. C-222 is among the most important banking legislation that we have had since Confederation. There are many reasons for this. But, one of the important reasons is that it includes a number of measures that should make the banking system more efficient; it would tend to remove restrictions. I am heartily in favour with the spirit of such measures and I support many of the individual measures themselves. At the same time I think there are some changes that should be introduced into the bill in order to achieve the objectives of the bill more effectively. I am going to approach my summary of the brief from the point of view of the major points I would like to make.

One thing worries me a bit and that is that some of my suggestions may appear too novel or too radical. I would straight away like to say that I do not think they are very radical. I do think they would lead to a more efficient banking and financial picture generally. Therefore, I would hope that they would be viewed as being changes that make good sense.

Now, I think there are perhaps half a dozen major points I would like to make. The first one is that I think the Bank Act should be amended to enable existing institutions such as trust companies and loan companies, under certain conditions, to apply for bank charters. This, I think, would remove legal obstacles to the natural evolution of such institutions. It would increase competition in the financial system. It would improve the financial services available to the small saver or investor. And, I think it would enable Parliament to honour its moral obligation to assist non-bank institutions to cope with increased competition from the banks that will arise from the amendment to the Bank Act. I stress the point that this kind of change, permitting existing institutions to apply for bank charters under certain conditions, is completely within the trend of the evolution of the Canada financial system. It is completely consistent with the

evolution of the Canadian financial system. I would remind you that, if you look back over the history of Canadian financial institutions, there are many instances where existing institutions have had to adapt themselves to change. There are instances where legislation made such change possible. I can point to the evolution of the building societies which before Confederation were quite important in this country. They had to change. They had to become loan societies, mortgage loan companies and legislation explicitly permitted that change. Then in the 1880's began the trust companies. They had one great advantage over the building societies, and that is that they had fiduciary powers. And, because of this advantage, they began clearly to be superior to the mortgage loan companies with the result that in the 1920's, as I am sure a number of you recall, a number of such loan companies transformed themselves into trust companies. I would emphasize that legislation permitted such a transformation. We are now to the point where both, because of the change in character of trust companies and loan companies, principally they are taking deposits, including checking deposits, and because of changes in the bank bill that will permit the banks to sell debentures and make conventional mortgage loans, the inherent differences between these institutions are diminishing. Yet at the same time present legislation would not permit trust companies and mortgage loan companies to apply for bank charters because their current assets and liabilities structure would not fit properly. I think, therefore, it is very important that a new section be introduced into this bill that would outline the conditions under which trust companies and mortgage loan companies could apply for bank charters and I talk about this in detail in my brief.

The second point I would like to make is this. The 6 per cent interest rate ceiling should be removed gradually by raising it by one half per cent per annum for five years and then removing it completely. And, I would add, this process would begin immediately. It does not, to me, make any sense to wait until interest rates are low to remove the interest rate ceiling. Why? Because it is when interest rates are low that company profits are in a weak position, and the profits of people who borrow from banks are in a weak position. I would think one should affect this adjustment when profits and business are good. And that moment is when interest rates are high. In addition, I should add there is just reason to argue in favour of a gradual removal of the interest rate ceiling to give competing institutions time to adjust and to give borrowers time to adjust. These are the considerations which lead me to recommend that the 6 per cent interest ceiling should be removed gradually but that such removal should begin immediately.

The third point I make is I think it is most important that the bank bill include provisions requiring full interest rate disclosure. I would simply emphasize this point by saying that in my view if such provisions are not included then the ceiling on loan charges should not be amended. I would add also at this point that the whole concept of the interest ceiling as such is being made less meaningful day by day because of the existence of minimum balance requirements for people who borrow from banks. The 6 per cent ceiling is not what money costs people who borrow from banks who are required to maintain minimum balances so that there is a certain illusion about the 6 per cent ceiling. It is in the act but in practice, in many instances, it does not mean anything any more. Something must be done to clarify the whole matter of the interest rate



ceiling and it must be accompanied by full and adequate interest rate disclosure provisions, in my view.

The fourth point is this. The permitted annual rate of increase of banks' debentures, I think, should be raised to 15 per cent of capital and rest for a period of 10 years. The present intended increase is roughly 2 per cent. It seems to me this is much too conservative an increase. There is no reason why the move of the banks into debenture financing should be that slow, particularly if my other recommendations were viewed favourably.

My fifth point is this. The split cash ratio, namely, 12 per cent for demand deposits and 4 per cent for savings deposits should not be introduced, in my view. Instead I would recommend each bank should be required to indicate in advance what cash ratio it wishes and intends to maintain in the year ahead. This would adequately serve monetary policy and would recognize much better than the split cash ratio the differences that exist among banks. You see the point really is that you can justify the split cash ratio only on grounds that there are some differences between banks; that some banks hold more savings deposits in proportion to their total deposits than other banks. This is a good point, but the point is that the differences between banks on the asset side are just as great as those on the liability side. Yet, the split cash ratio recognizes only the differences on the liability side.

The other point, too, is that in my view the arbitrary decision as to what will constitute a savings deposit and what will constitute a demand deposit, will, under present banking conditions, make very little sense at all. What would you call a two-day term deposit on which interest is paid? Is it a demand deposit or is it a savings deposit? It is a very short term deposit. I think that no satisfactory definition of what constitutes a savings deposit and what constitutes a demand deposit can be arrived at. For this reason, too, I would prefer the approach that I take to defining what the minimum cash ratio should be for a bank.

My next point is that provision for a secondary reserve ratio should be eliminated from the bill entirely because it introduces an unnecessary rigidity into the Bank Act at a time when attempts are being made to reduce legislative rigidity.

My seventh point: foreign bank agencies should be permitted but initially only for a trial period, and the eighth point, the prohibition against loans on the security of all bank stocks should be amended to include only loans against the banks' own stock. I was interested in this provision because it has existed in the Bank Act since the 1870's. I examined the contemporary press of that period for reasons why it was introduced in the first place. There can be no doubt that the banking system at that time was more or less a jungle and that the most fantastic things were happening in the capital market. Bank stock was the major stock on the stock market. All the speculators in the country, none of whom was controlled in any meaningful sense, were engaging in very curious practices with respect to trading in bank stocks. That world no longer exists and yet this provision with respect to making loans against collateral of bank stock has persisted over the years. I do not think it is necessary any more and would recommend that it be amended the way I have suggested in my brief. Thank you Mr. Chairman.

The CHAIRMAN: Thank you, Dr. Neufeld. I would recommend to the Committee that we discuss the topics raised by our witness in his brief in the following order. First, his proposals regarding extending bank charters to other deposit taking institutions. I suggest we could logically include with that his views on deposit insurance. Then I suggest we move on from there to the specific topics he has raised beginning with the interest rate and with that I would include his earlier discussion at the beginning of his brief regarding interest rates because it is part of the same general proposal as well as Dr. Neufeld's views on disclosure of interest rates. Again he seems to bind this up into the same general package. We will move on from there to debenture borrowing, then combining our discussion of his proposals four and five on the general area of reserve ratios.

From there we will move to his views on foreign bank agencies and we might, at that point, wish to ask him something about the operation of foreign banks in general in Canada; finally, his last point dealing with the prohibition of loans against banks stocks.

Does this seem to be an orderly way of dealing with the views put forward by our witness this morning? If that is the case and we are agreed on this, I would invite members of the Committee to signify their desire to place questions. I recognize first Mr. Lambert followed by Mr. McLean and then Mr. Cameron, and Mr. Laflamme. I will note them down.

Mr. LAMBERT: Mr. Chairman, with regard to Professor Neufeld's proposition that the near banks be permitted to move into the field of chartered banks, does he feel satisfied that a meaningful number of the present near banks would want to come in and give up whatever privileges or characteristics they have under their own particular incorporation to assume the liabilities and responsibilities of the Bank Act which becomes their charter?

Mr. NEUFELD: I think there are two points there. The first point is, of course, the fortunate aspect of my approach is that any institution that did not want to come in would not have to come in, which distinguished it from the approach which says let us arbitrarily define something as a bank and force it to come in.

Mr. LAMBERT: But as a corollary, you would agree that the organizers or the backers of any near bank today have the same privilege as anyone else of coming in and applying for a bank charter?

Mr. NEUFELD: This raises the second aspect of your initial question and that is would they want to come in or would they wish to forgo any privileges they now have in order to assume the responsibilities outlined under the Bank Act. The point I would make here first of all, is that there are some differences but these are not vitally important and special provision should be introduced to accept those banks under the provisions of the Bank Act which would, on the face of it, preclude them from applying for charter. Where are these areas of difference? They are mainly on the structure of assets. All these institutions make many more conventional mortgage loans than even the present Bank Act would permit. The other difference is on their liabilities. All these institutions issue more debentures or guaranteed investment certificates than is envisaged at present under the Bank Act. The third point is trust companies enjoy fiduciary powers which are denied to the banks. My point is that since this bill does in fact accept the principle that banks should engage in conventional mortgage lending

and should be permitted to issue debentures, this distinction between banks, trust companies and loan companies is therefore being removed. It will take a while to remove it entirely but in principle it is now being removed. So the only real difference we are left with is fiduciary powers. My view on that is, I think, a very common sense one, namely, permit trust companies that now enjoy fiduciary powers to retain a monopoly of such fiduciary powers for the next ten years; that is, from now until the next revision of the Bank Act, so as to assist them in transforming themselves into banks if they so wish to do. These are, I think, the major differences that might cause trouble.

Mr. LAMBERT: On the other hand, do you think it would be possible so to divide the Bank Act that you could have a category of banks; some chartered and some non-chartered, but that the category of non-chartered banks would not have the Bank Act as their particular charter but there would be your supervisory powers. This is what you are driving at, I think.

Mr. NEUFELD: What I see is that for ten years or so there would be differences between existing institutions that apply for bank charters and existing banks; and, that a separate section of the Bank Act would deal specifically with the fact that there would have to be differences for a ten year period between those institutions and others. I see no great obstacle in introducing a special section in the Bank Act would specifically deal with the fact that such differences would have to exist for a temporary period.

Mr. LAMBERT: Do you feel there would be any particular value in the name and reputation of a chartered bank?

Mr. NEUFELD: I think this is of tremendous importance.

Mr. LAMBERT: Do you think these near banks would tend to come in and be entitled to that name and reputation?

Mr. NEUFELD: I include in my brief the phrase, I think, that they would have to meet certain fairly stringent financial requirements which should be defined in advance. But, I think it would be easy to name off, if one wished to do so half a dozen or a dozen existing non-bank financial institutions who surely should meet no obstacles in applying for and obtaining a bank charter. But I think they should meet fairly stringent financial standards that should be defined in the Bank Act.

Mr. LAMBERT: Could you give us some idea of what they should be?

Mr. NEUFELD: These would relate, I would think, essentially to such matters as the reserve, capital and reserve of the institution, I think it would probably have to include provision that they would have to undergo a most thorough audit before a charter would be granted to them.

The CHAIRMAN: And after?

Mr. NEUFELD: After that they would be subject to the Inspector General of Banks.

Mr. LAMBERT: As a last question, Mr. Chairman; do you think that the act and the operations of both the chartered banks and the near banks could be improved by a definition of banking in the act? Have you come up with any ideas about a definition of banking?



Mr. NEUFELD: Yes, I have. I would say that a financial institution is a bank to the extent that its liability instrument is used as a medium of exchange. I think that to understand that this is the correct definition of banks, one has to reflect a bit on the nature of the evolution of banks. You may wonder why it was that we never had any discussion as to what was a bank in Canada for the first hundred years or so of our existence. The reason is simple. It was that everyone knew that a bank was a financial institution that issued demand notes. No one quarrelled about this. But it was in 1934, when the issue of notes right began to be taken away from the banks, that problems arose as to how do you define a bank. But the distinguishing characteristic of what a bank note was that it was a medium of exchange. When the banks first began it was the important medium of exchange. It was the money of the country. When over the years the bank deposit replaced the bank note as the way people did business, and then this definition of what constituted a bank began to be fuzzy because first bank notes began to decline and secondly the right to issue bank notes was taken away from the banks. But this should not hide the fact that the distinguishing characteristic of the bank was that it issued something that was used as money, as a medium of exchange, as a checking deposit. That is why I think a bank has to be defined in terms of the use of this liability instrument as money or medium of exchange.

Mr. LAMBERT: Thank you, Mr. Chairman.

The CHAIRMAN: Thank you, Mr. Lambert. Dr. McLean?

Mr. McLEAN (*Charlotte*): Mr. Chairman, I would like to ask the professor does he think a finance company should apply for a bank charter?

Mr. NEUFELD: I do not think that finance companies would be eligible for bank charters, for the simple reason that the liability side of their balance sheet does not in any way look like a bank's. They do not, in fact, solicit deposits from the man on the street.

The CHAIRMAN: What about a group like the Prudential Finance which, in effect, seem to have been doing that.

Mr. NEUFELD: They tended to issue small notes. They did not take deposits from the man on the street. They issued small notes to small holders. I would, of course, emphasize that new banks would have to meet the same sort of financial requirements, in terms of parliament, say, and inspection on the part of the Inspector General of Banks as would the existing banks.

Mr. McLEAN (*Charlotte*): You say you thought perhaps trust companies should apply for bank charters? Well, should banks apply for trust company charters?

Mr. NEUFELD: I would think the only reason why banks might want to apply for trust company charters is in order to do fiduciary business, because they are now already being given the right, or they will under this bill be given the right, to issue debentures and to make conventional mortgage loans. So that difference will gradually disappear between the trust companies. But the bill does not foresee their getting fiduciary powers. So this the banks might regard as desirable. My view is that I see no reason why after a transition period of, say, ten years, all existing chartered banks should not be given the right to do fiduciary

business. But I think for the first ten year period, to ease the transition of trust companies into banks, the trust companies should enjoy a monopoly on fiduciary business.

Mr. McLEAN (*Charlotte*): Has there not been a tendency in the past to keep these things apart, the trust companies and the banks?

Mr. NEUFELD: Yes, there has been. This difference has, however, steadily, through the natural evolution of the development of the market, diminished. I think it is perfectly right to say that when our financial institutions first began there was a deliberate attempt on the part of legislators to distinguish between them. If I may give one example, in the early days of the trust companies there were strong attempts made to prevent trust companies, on the one hand, from taking deposits because people began to say, if you permit them to take deposits or issue demand notes then they are banks and we did not want them to be banks. On the other hand, they were not permitted to issue debentures but the curious reaction to this was that they were permitted to issue guaranteed investment certificates. For many years the business community, and I think the legislators and so on, convinced themselves that there was some significant difference between investment certificates and a debenture. In fact there is no significant difference. So I would emphasize that while the attempts were made to distinguish the two institutions both on the liability side and the kind of business they did, in fact this distinction has persisted and consistently been diminished over time and today the trust companies can take deposits which it was originally thought they should not do and they are now, in effect, issuing debentures which too, originally it was thought they should not do. On all this, I might say I think it is a very sensible evolution of the financial system.

Mr. McLEAN (*Charlotte*): You state, I believe, that the 6 per cent ceiling should be taken off. Now, with reference to interest rates, this does not make more credit available, apparently?

Mr. NEUFELD: No.

Mr. McLEAN (*Charlotte*): Well, then we would just have the banks and everybody else bidding against themselves. I think they have had that situation in the United States where one institution was bidding against the other and it has more or less created chaos in the financial world. How would you go about that? Some people think if you keep the interest rate at 6 per cent it will have an influence in keeping interest rates more or less steady. In the United States I believe they have a ceiling now. But then they drive them to borrowing in Europe and where they were borrowing these Eurodollars at  $5\frac{3}{4}$ , now they are paying  $8\frac{1}{2}$  and 9 per cent for them.

Mr. NEUFELD: Yes.

Mr. McLEAN (*Charlotte*): Should there not be some world-wide control of interest rates.

The CHAIRMAN: I will permit Dr. Neufeld to answer the question but I would remind the Committee they have, in effect, agreed that the discussion of interest rates be dealt with separately and at the present time—

Mr. McLEAN (*Charlotte*): Although you just went down the line. I thought you were permitting questions to go down the line.

The CHAIRMAN: No, I thought we were following our previous procedure of dealing with the witnesses' briefs in the order of topics. But would you like to answer that question at this point so we will not have a hiatus in the discussion.

Mr. NEUFELD: I think one should be very clear on the advantages that arise out of removing the ceiling. The advantage certainly is not that it will make more credit available, and in a period when the economy is fully employed that is just as well. But the advantage is that it should improve the way credit is allocated. I think it is fairly certain that removal of the ceiling would push some of the large bank borrowers out into the capital market. Indeed, I am led to believe that there might already be instances where merely because of the use of compensating balances some borrowers have gone to the market. But if this sort of thing happens there would be more credit available to the small and medium size borrower, not merely for current purposes but also of the medium term nature. This is the great advantage to be achieved through removal of the ceiling: a better allocating of the existing amount of credit.

The CHAIRMAN: Doctor, I would ask you to withhold further comment on this very important matter until we get to that stage of your brief.

Do you have any further questions, Dr. McLean, on Dr. Neufeld's proposal to permit loan and trust companies to obtain bank charters and also the related topic, I think, of deposit insurance?

Mr. McLEAN (*Charlotte*): I have a question on deposit insurance.

The CHAIRMAN: I suggested we deal with these two topics together.

Mr. McLEAN (*Charlotte*): Now or later? Right now?

You say that you favour deposit insurance?

Mr. NEUFELD: Yes.

Mr. McLEAN (*Charlotte*): Now, the chartered banks have federal inspection and they have outside inspection and they have their own inspection. Why should they have deposit insurance?

Mr. NEUFELD: Why should the chartered banks have deposit insurance?

Mr. McLEAN (*Charlotte*): Yes.

Mr. NEUFELD: I think it is fairly certain that the chartered banks would not need deposit insurance. I do think, that, because of the position of the chartered banks, because of the inherent advantages they enjoy through having access to emergency funds from the Bank of Canada, for example, there is something of a *quid pro quo* involved here. I would favour the chartered banks having a contribute to a deposit insurance organization because they, in fact, do have certain privileges that other financial institutions do not have. This is not a very scientific approach to the problem, I agree, but all in all I think that it would not be too bad for the chartered banks to contribute to a deposit insurance fund and lower somewhat the cost of insurance to other institutions in that way.

Mr. McLEAN (*Charlotte*): Why should they have to pay for something they do not need?

Mr. NEUFELD: Because I think they are getting other privileges for which they are not paying.



Mr. McLEAN (*Charlotte*): Yes, but on the other hand they have deposits with the central bank which they do not get any interest on; is that not so?

Mr. NEUFELD: That is true, they do. But, in addition, they have all the advantages of having access in emergency cases to central bank funds and they have the tremendous advantage of using the name "bank", "chartered bank". This is denied other financial institutions.

Mr. McLEAN (*Charlotte*): Then, you believe they should pay for something for their competitors?

Mr. NEUFELD: I beg your pardon.

Mr. McLEAN (*Charlotte*): It does not look reasonable.

Mr. NEUFELD: Well, only if you deny my other view, which you certainly have a perfect right to do, that they are obtaining other advantages not open to non-bank institutions.

Mr. McLEAN (*Charlotte*): Well, none of the non-bank institutions are federally inspected. You can see what is happening all around us. I think if they are inspected federally they should not pay. The government put up \$100 million of funds why should there be any losses if they were federally inspected?

Mr. NEUFELD: I think that in itself is a perfectly good comment. I think every time you have a major bankruptcy—if you do have a major bankruptcy—of an institution inspected federally, there is something wrong with the inspection; I could not agree with that more. I would like to make this point, that my view with respect to deposit insurance should not be separated from my suggestion that non-bank institutions, under certain conditions, should be permitted to apply for bank charters.

The CHAIRMAN: So there would not be a hiatus in the total effect.

Mr. NEUFELD: That is right.

The CHAIRMAN: I sensed, Dr. Neufeld, that this was implicit in your approach.

Mr. NEUFELD: Yes.

The CHAIRMAN: It is one reason I suggest to the Committee that we take these two topics together.

Mr. NEUFELD: Yes.

The CHAIRMAN: At the last meeting, I suggested that perhaps an approach to the anticipation of banks in deposit insurance would be to wipe out their present obligations to pay the special assessment for the services of the Inspector General of banking, and merely have them pay the premiums for the deposit insurance scheme. These profits, of course, would be reimbursed under the returns of the insurance fund.

Mr. NEUFELD: Well, it might be conceivable; I had not thought of it.

The CHAIRMAN: Surely the banks would not have an undue share of the costs.

Mr. NEUFELD: It is conceivable.

The CHAIRMAN: Do you have any further questions on these two topics, Dr. McLean? If not, I will recognize Mr. Cameron, followed by Mr. Laflamme and Mr. Clermont.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Dr. Neufeld, do I understand your proposal regarding the trust and loan companies being permitted to apply for charters, as, in effect, envisaging at the end of ten years an expanded banking industry with more institution privileges. They would at the end of ten years have common functions, then I presume they would have common obligations regarding cash reserves, and so on.

Mr. NEUFELD: Yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): At the end of ten years you would have the same obligations.

Mr. NEUFELD: Yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Now, could I turn to your definition of banking and ask you if you would agree with the definition we were given on Tuesday by Dr. Slater of Queen's University, which went a bit further than yours, it seems to me. He deposited as the two most important criteria for a definition of banking, the one you gave this morning that their obligations became part of the money supply, but also that their operations affected the total money supply.

Mr. NEUFELD: Well, I think that is just simply one point, because if their obligations are part of the money supply, their operations will affect the money supply. So, I think my definition, implicitly includes the other part of the definition.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Has it occurred to you, Dr. Neufeld, that if the federal parliament embodies in legislation a definition of banking, then this in effect will be an assertion of federal authority over all institutions who meet these two criteria. Have you given any thought to the position of institutions which are licensed provincially?

Mr. NEUFELD: Yes, I have; I think that a judicial decision would have to be made whether the new definition of the bank was consistent with the federal powers over banking in Canada. I think it is problematical whether or not that would be a favourable decision in the sense that it would in fact be viewed as including provincially incorporated institutions. It is partly because of this concern that I favour my approach, which is to permit any financial institution—provincial or federal—to apply for a bank charter and to receive a charter if it meets certain requirements. All aspect of compulsion is then removed. Furthermore, I would say, that since the relative amount of financial claims that is essentially money that is issued by non-bank institutions, is still very small in relation to the total, I do not think it is a crucial issue from the point of view of monetary control. I accept all the theoretical aspects of the problem; that is, that there are non-bank institutions that issue money today. But I would just simply say that from a practical common sense point of view, the amount that they issue in relation to the total is still so small that it does not matter for purposes of monetary control; which is, I think, another argument in favour of using not the compulsion approach, but simply an approach that permits a natural evolution of institutions.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Have you taken into consideration the rate of growth of non-banking institutions in the last ten years, and considered what the situation may be at the time that this Bank Act, we are passing now expires in ten years from now? Do you not think it is possible that by that time there may be an increase in the number and the size of provincially licensed institutions which conform to the criteria of banks, as you have set it forth, which might very well be an obstacle in the way of federal monetary control?

Mr. NEUFELD: I do not think so, for this reason: the growth of non-bank institutions, that has taken place, I think has arisen not through the growth of essentially money financial claims issued by non-bank institutions; but rather the growth of other kinds of claims issued by non-bank financial institutions.

The other point I would make is that this bank bill will make the banks more competitive by permitting them to issue debentures, and by permitting them to make conventional mortgage loans. Therefore, I think, and particularly when the restriction on debenture issues is eased—as it should be in time—it is quite conceivable that in ten years time the non-bank institutions will face very substantial competition from the banks. The fact that non-bank institutions have grown rapidly under conditions of severe restriction on the operations of the banks does not mean that they will continue to grow rapidly when the restrictions on the banks are removed. Indeed, when this bank bill works itself out fully, there are really very few unique advantages remaining to the loan and trust companies. Therefore, if the banks show any kind of initiative at all, in ten years time I think they should be in a very strong competitive position. May I emphasize that I think this is the way the evolution of the financial system should go.

The CHAIRMAN: Do you think the banks will show this kind of initiative?

Mr. NEUFELD: With all these bankers facing me I do not know what I should answer to that.

The CHAIRMAN: You have a certain parliamentary immunity with respect to anything you say here, so feel free to speak very frankly.

Mr. NEUFELD: Well, I think that part of the reason for their slow growth has been that they have not shown sufficient initiative in the past. It is an open question now, whether they will take full advantage of the changes that are now included in this bill.

Mr. LEBOE: Mr. Chairman, I have a question. Have you given consideration, Mr. Neufeld, to the possibility that we should not be waiting ten years; that we should split it in half, shall we say, before we reach a review of the Bank Act again?

Mr. NEUFELD: I think that there are other aspects of changes which would strongly support the view that you take; particularly if anything is done with respect to foreign agencies. But with reference only to the things we have discussed, I think—and we are really discussing long term evolutionary changes—that probably a ten year span would be quite sufficient.

Mr. LEBOE: Thank you.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): To come back again to the effect of embodying a definition of banking in legislation—I suppose this is really



not a question I should propose to an economist, but perhaps to a lawyer—have you given any consideration to the possibility that although there may be some doubt that the court would rule that this definition of banking would affect provincially licensed institutions; would there be the same doubt about its effect on federally incorporated trust and loan companies? Would they not almost automatically be obliged to seek bank charters and come under the provisions of the Bank Act?

Mr. NEUFELD: I just am not confident enough, about what the judicial decision would be, to say. I suspect that the decision might be based on considerations quite apart from provincial or federal incorporations. So, I think it is just questionable whether one would get an economically acceptable decision from the courts.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I gather you take it that the principal obstacle in the way of the banks competing successfully with the near banks, has been the prohibition, up to now, of the issuance of debentures.

Mr. NEUFELD: I would say that it is the prohibition against the issue of debentures, the interest rate ceiling—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But you told us just now that the interest rate ceiling really was not—

Mr. NEUFELD: In very recent years.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It really is a dead letter.

Mr. NEUFELD: But I would include it, as whatever influence it has, it is in the direction that would slow the growth; whether it would do it very much or not is questionable. But the three points are the restriction on the issuance of debentures, the prohibition against conventional mortgage lending on the part of the banks—and I would regard that as very important—and, thirdly, the interest rate ceiling.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Have you any idea at all of what would be considered by the banks as a wise and prudent level of debenture issues in relation to their reserves, and in relation to their capital?

Mr. NEUFELD: Well, if you look at the trust and loan company legislation, you will find that over the last 50 or 60 years there has been a continuing increase in the leverage of those institutions, a continuing increase in the amount of debentures in relation to capital; and it is now very large. In view of developments there, it is almost to the point where effective control from that point of view, no longer exists, in the case of the trust and loan companies. I would think that the same sort of principle would apply in the banks, that is, that in fact after a period of transition there would probably be no need for any specific control on the amount of debentures that banks issue.

The CHAIRMAN: I would like to interrupt at this time to remind the Committee that we have the matter of debenture borrowing by banks as a separate topic. Thank you, Mr. Cameron.

(Translation)

The CHAIRMAN: Now, I will give the floor to our vice-Chairman, Mr. Laflamme.

(English)

Mr. LAFLAMME: Do I interpret what you said correctly that near banks or other financial institutions should be allowed to become banks as long as they receive deposits?

Mr. NEUFELD: As long as they meet certain defined financial standards. I think that it is quite conceivable that one such standard should be the nature of their borrowing business; particularly whether or not they were in the deposit business.

Mr. LAFLAMME: You say certain—

Mr. NEUFELD: Adequate capital and adequate reserves.

Mr. LAFLAMME: Would it not be only the applications of the Bank Act?

Mr. NEUFELD: No, because if you applied the Bank Act as it now stands, or even as it will be after this revision, then it would be impossible for even the strongest non-financial institutions to get a bank charter. Clearly, they would not be eligible because they would have too many debentures outstanding, and they would probably have too many residential mortgage loans on their books, and they would, for these reasons, not meet the existing requirements of the Bank Act.

Mr. LAFLAMME: But along this line, how would deposit insurance bring these financial institutions under the control of, let us say, the Minister of Finance, or the inspector of banks?

Mr. NEUFELD: Well, to the extent that provincial institutions were to apply for deposit insurance, I think it would partially serve the purpose of improving the effectiveness of control of such institutions. But I would emphasize that the one great disadvantage of deposit insurance is that it does not really assist very much in the evolution of existing institutions, because it does nothing to enable existing institutions to evolve into banks and to get the full privileges of being banks. Therefore, while it is good in itself, and will increase probably the efficiency of supervision of the institution, and perhaps even encourage the growth of some new institutions, I think it will contribute very little to the natural evolution of the financial system into a more efficient one.

Mr. LAFLAMME: Then, how would you define the main purpose of the proposed deposit insurance act?

Mr. NEUFELD: I think, from an economic point of view—I am going to ignore the fact that it might lead to better supervision of such institutions—I would see the main advantage to be the one of reducing the difficulties for small institutions to gain the confidence of the public, and, therefore, to be established and to grow and to compete with existing institutions.

Mr. LAFLAMME: Then, getting back to the other financial institutions, we were told here by some other witnesses that the RoyNat had served in many areas where the banks did not specialize, where the banks had never worked and could not work. Would you say that an institution like RoyNat which has specialized in many other fields than the usual activities of the banks should become a bank?

Mr. NEUFELD: I would doubt it, because I would think that the character of its liabilities does not begin to make it a bank, by almost any definition that one would choose. At the same time, I would again emphasize that whether or not it should be permitted to become a bank would depend on the specific financial standards that would be established. I would go on to say that I think if the banks had had conventional mortgage lending rights to begin with, and had had the right to issue debentures, it is quite conceivable that RoyNat would never have been formed.

The CHAIRMAN: What will it mean to RoyNat if the banks have these powers?

Mr. NEUFELD: I think one would say, other things being equal, that the need for RoyNat when the banks have complete freedom to issue debentures and make conventional mortgage loans, would be somewhat less than the need has been in the past. I would think the need in the past was quite substantial in view of the restrictions on the banks.

The CHAIRMAN: Yes, Mr. Laflamme?

*(Translation)*

Mr. LATULIPPE: A supplementary question, Mr. Chairman.

The CHAIRMAN: An additional question, Mr. Latulippe?

Mr. LATULIPPE: Are the banks now entitled to issue debentures?

The CHAIRMAN: It is not in the law.

*(English)*

Mr. NEUFELD: No; they have always interpreted the legislation as meaning that they are not permitted to issue debentures.

*(Translation)*

Mr. LATULIPPE: They are able to buy debentures but they are not able to issue them?

*(English)*

Mr. NEUFELD: There is no restriction on their buying debentures; that is, debentures issued by other institutions; just as there is no restriction on their buying mortgages. But there is a restriction, the way they have interpreted the legislation, on their selling debentures to raise money.

*(Translation)*

The CHAIRMAN: And now I give the floor to Mr. Clermont.

Mr. CLERMONT: Mr. Neufeld, you mention that the financial institutions that are not banks should be considered as banking institutions. If I understood you well, to be accepted as banking institutions they would have to qualify under the present Banking Act?

*(English)*

Mr. NEUFELD: I think that they would have to qualify under banking legislation of the future. But the problem is this: because of the nature of present



operations and the nature of the present Bank Act, they simply could not qualify at present. This makes it necessary that there be a transition period when the nature of their assets and their liabilities would be different from the nature of the assets and liabilities of existing banks. At the same time there would be no need to have any different kind of supervision of those new banks from existing banks. The Inspector General should look at them just as closely as he would at existing institutions.

*(Translation)*

Mr. CLERMONT: But would these non-banking financial institutions have to make a deposit with the Bank of Canada as chartered banks have to do under the present Banking Act or under the revised Bank Act, Bill C-222?

*(English)*

Mr. NEUFELD: I would certainly think that if such institutions were permitted to receive charters they should, from the beginning of the granting of the charter, adhere to the same cash reserve requirements as existing banks. I would point out, however, that my view of what such cash requirements should be is different from that reflected in the present bank bill. But I see no reason why, from the day that they receive the charter, they should not adhere to the same cash reserve ratio requirements as existing banks.

*(Translation)*

Mr. CLERMONT: In your first reply to my first question you said that perhaps in the present Act, these near-banking institutions would not qualify but might qualify under Bill C-222. What do you do with Clause 52 (d) of the projected Bill C-222, that would prevent any stockholder or company to hold more than 10 per cent of shares? I do not know if you are familiar with the Bank of Western Canada proposals where it was shown that one of the provisional directors or his group held, I think, between 20 and 25 per cent of stock if not more?

*(English)*

Mr. NEUFELD: Well, again I would say that in the matter of interlocking directorships, I see no reason why such new banks—that is, existing institutions that have applied for charters—should not adhere to the same provisions as those which existing banks have to adhere to. In other words, in cases where there were interlocking directorships, which would be in contravention of the present Bank Act, they would have to get rid of them before they would get a bank charter.

*(Translation)*

Mr. CLERMONT: But it is not a question just of interlocking directorships but of the percentage of shares that might be held. Are not the trust companies or near-banking institutions obliged to have only a certain percentage of shares, or is the percentage of shares not limited?

*(English)*

Mr. NEUFELD: Well, again, I think this is one area where there would not be any great difficulty, because if parliament decides that it is not a good thing for

chartered banks to have more than a certain equity interest in other financial institutions; then I see no reason why that same requirement should not be imposed on any existing financial institution that applies for a bank charter. I agree that it might well mean that they would have to sell out their interests in some existing financial institutions; but I see no reason why exceptions should be made on those grounds. After all, this is a change that an institution can make reasonably quickly—over two or three years time—if it wishes to do so. In other words, I would emphasize that for an institution to obtain a charter it would have to accept the obligations of such charters. But my main worry was in other areas, where rapid change to make non-bank institutions conform with the present provisions of the Bank Act, cannot come quickly. This is particularly on the matter of the character of their assets and the character of their liabilities. I think that is where the problem arises and where there must be a period of time to permit this transition to take place. I do not think this would be the case with respect to either interlocking directorships or equity ownership of existing institutions.

*(Translation)*

Mr. CLERMONT: According to your definition, I would like to know if the Caisses Populaires and the Credit Unions are considered as banks? Are they banks, in fact?

*(English)*

Mr. NEUFELD: I would say that credit unions and Caisses Populaires are banks to the extent that their liability instruments are used as a medium of exchange. Since it is well known that a fair portion of those liabilities are used as a medium of exchange, then to that extent they most certainly are banks from the point of view of an economist.

*(Translation)*

Mr. CLERMONT: As you are aware, we know that Caisses Populaires have a provincial grant. I know that the Caisses Populaires in Quebec have more than 1.5 billion in deposits.

*(English)*

Mr. NEUFELD: Yes, I agree they do, and to that extent in an absolute sense they are very important and I think they serve a most useful function, both the Caisses Populaires and the credit unions. There is nothing I would recommend that we should reduce their effectiveness. I think that this is one of the very desirable aspects of my approach. I would not interfere with the development of such institutions; whereas the approach that begins by defining a bank in some arbitrary way, which requires one to impose controls even on the Caisses Populaires and the credit unions because some parts of their operation an economist would define as banking, that approach, I think, would tend to be too restrictive. I cannot even see how it could be operational, considering the fact that each credit union local and each Caisse Populaire is a fairly independent kind of organization.

(Translation)

Mr. CLERMONT: Concerning the plans which are being proposed by the Government for deposit insurance you answered Mr. Laflamme by stressing the supervision. Do you think that near-banks should be considered as banks, that they need certain regulations? Do you think that supervision or control is important for institutions which sell shares to the public? Because I read the brief by Professor Binhammer I believe, concerning FDIC at page 9, I can read:

(English)

Its success, to date, in making the system failure-proof is, in large part, the result of its supervisory and examining—

Mr. NEUFELD: Yes, I think that the success of the Federal Deposit Insurance Corporation is largely dependent on the fact that along with the guarantee of deposits there was a system of supervision and inspection examination, I think that is true. At the same time, I think that the Federal Deposit Insurance Corporation face completely different conditions from those we would face in Canada. That began with a unit banking system where the whole banking system was broken up into small units and control and supervision there really meant control and supervision of a very large portion of the banking system. In Canada those institutions that would benefit from the Federal Deposit Insurance Corporation, that would benefit from the guarantee of deposits form a much smaller portion of the total banking system than was the case in the United States in the 1930's when it was introduced.

(Translation)

Mr. CLERMONT: My last question will relate to the incorporation of banks, Mr. Chairman. As a professor do you believe that a deposit insurance plan would enable the two new institutions which obtained charters from Parliament at this session to do banking to obtain deposits. Would it be easier for them to obtain deposits from the public?

(English)

Mr. NEUFELD: I think there is no doubt at all that it would make it easier for those new institutions and other new institutions in future to take deposits from the general public. I think that the public frequently is very reluctant to entrust its money to a new and untried institution and if the public was guaranteed the security of its money up to a certain amount, then surely the reluctance should be substantially diminished.

● (12.17 p.m.)

(Translation)

Mr. CLERMONT: Mr. Chairman, I would like to ask a supplementary question concerning this insurance plan. Are you satisfied with a total of \$10,000 or an amount over \$10,000 concerning this deposit insurance?

(English)

Mr. NEUFELD: I am quite satisfied with the \$10,000. I think that anyone who has more than \$10,000 to put into one institution should know what he is doing.



We are really worried about the great proportion of people with much smaller amounts than that who keep their money in financial institutions.

The CHAIRMAN: Now, Mr. Gilbert followed by Mr. More, Mr. Wahn and Mr. Fulton.

Mr. GILBERT: Mr. Chairman, most of my questions have been asked by other members. This question is just a development of the answer that Dr. Neufeld gave to Dr. McLean.

In advancing your proposition, Dr. Neufeld, that near-banks should be granted charter extensions the same as banks, Dr. McLean asked about finance companies and the distinction you made was that they were not deposit-taking institutions.

All that a finance company would then have to do is change into a deposit-taking institution and then it moved qualify for a charter.

Mr. NEUFELD: No, that would not be the case. I have indicated that I would require such institutions to meet certain general financial standards, and I would think that the other aspects of those standards would be much more important than whether or not they had a certain volume of deposits on their books. If, however, they met certain recognized financial standards which would make them just as sound a financial institution as existing banks, under those conditions there would be no objection to their obtaining a bank charter.

Mr. GILBERT: Thank you Dr. Neufeld.

Mr. MORE (*Regina City*): Many of the questions I had in mind have been answered, but I am interested, Dr. Neufeld, in bringing the near-banks into chartered bank corporations. You suggest, I take it, that the present proposals do not permit this to the extent you would like to see it?

Mr. NEUFELD: I think that the present proposals would make it literally impossible for the sounder non-bank financial institutions to obtain bank charters.

Mr. MORE (*Regina City*): And it is your belief that the present act should be such that it would permit them to come in and obtain charters? Do you consider that now is the time this should be done?

Mr. NEUFELD: I think now is the time that it should be done, because it will take at least ten years for them to evolve into banks in the sense that they would be able to comply with all the requirements of the Bank Act. The reason I think it should begin now is, first of all, that it will take a long while for this to work itself out and, secondly, that some of the changes in the bank bill will increase the competitive position of the chartered banks, and over the next ten or twenty years exert an increasing competitive pressure against some of these other institutions.

What I am suggesting is that we make it easier for non-bank institutions to evolve into banks to meet the kind of competition that they might well get, over the next ten or twenty years, from the banks under the new legislation.

Mr. MORE (*Regina City*): Do you feel that this is a better way of having more chartered banks in our financial operation than the incorporation of new companies who set up and comply fully with the present requirements which are laid down?

Mr. NEUFELD: I think it is a much better approach. I do not think there is essentially a shortage of banking facilities in Canada, but I think that it is desirable to remove obstacles that prevent existing institutions from naturally evolving in the future.

The other point is that I think by and large the optimum size of a financial institution is a pretty big one. I think that in the long term a one-branch bank, or a branch bank with few branches, is not an institution of competitive size and therefore it will become competitive only if it can grow big. Not only the evolution in our country suggests this but the evolution in many countries suggests this, that the efficient financial institution is a pretty big institution. I think it would be more desirable to permit the natural evolution of existing financial institutions than to try to introduce a lot of small new banks into the Bank Act, which would become efficient in an economic sense only after they became very large.

Mr. MORE (*Regina City*): And as this transition took place, would you then feel that there would not be development of new loan and trust companies as loan and trust companies in the future?

Mr. NEUFELD: I doubt that there would be many new loan and trust companies as loan and trust companies.

Now, here is a very interesting point in this area. At about the turn of the century, according to my research and compilation, we had about a hundred loan and trust companies in Canada. Then there was a period of consolidation, mergers, insolvencies, bankruptcies, and all the rest of it, so that by the 1930's we had a handful of them. There was this natural evolution in that area to fewer and larger institutions.

The same thing happened to the banking system. In the 1870's we had about 50 banks and now we have only a handful. Similarly, in the banking systems of many other countries, the move has been toward fewer and larger banks because this is the way in which efficiency seemed to be achieved.

Mr. MORE (*Regina City*): Would you feel that at the present time in the mind of the general public there is a great deal more confidence in chartered banks than any of our other financial institutions?

Mr. NEUFELD: I think there is more confidence in the banking system than in other financial institutions, although in this period of continuous prosperity I think the confidence in the other institutions has increased very substantially from the low point it reached in the 1930's.

Mr. MORE (*Regina City*): Do you think that is based on public knowledge of their operation, or on the fact that they pay higher rates for deposits?

Mr. NEUFELD: I think that it is a matter of rates. It is also the fact that in some areas those institutions provided a lot better service than the banks. For one thing, their hours were more sensible. They introduced more branches, too, which caused their growth. I think there were a number of individual forces that led to the rapid growth of the non-bank institutions.

Mr. MORE (*Regina City*): Do you think this public confidence is based purely on the fact that they hold a federal charter under the Bank Act, or is it based on

the operation of the companies who have these charters and that they have earned this because of their operation and the standards that they set in their operation?

Mr. NEUFELD: Of course it would be very difficult to determine why an individual person approaches the bank with a great deal of confidence, but I think the fact that they do have a federal charter and the very fact that they are essentially the only institutions that can use the word "bank" sets them apart. The fact that it has been a long, long time since a chartered bank has become insolvent is another factor. I also think that historically the banks have always been in a very strategic position; they have been at the top of the pyramid as far as all financial institutions are concerned.

I think that all these factors have led to the public, quite rightly, placing a great deal of confidence in the Canadian banking system. I certainly think the way in which they survived the 1930's influenced a lot of people's attitudes towards banks in Canada.

Mr. MORE (*Regina City*): Under your proposals, if accepted, for the next ten years you would have institutions as chartered banks that differed in their operation. Do you see no problem in this?

Mr. NEUFELD: No, I see no problem because my own view would be that there are a lot of non-bank institutions that in fact are just as sound and as efficient and as reliable as banks and yet they are not able to call themselves banks, and this is at a time when the banks' operations are becoming more and more like their operations.

Mr. MORE (*Regina City*): If they do become banks at this time, would the restrictions on the issuance of debentures, on the interest rates, and so on, apply to them. Is this your idea?

Mr. NEUFELD: I think that after a transition period of ten years there would be no need to make any legislative distinctions between the new banks and the existing banks, but I recognize that in the interim there would have to be differences.

Mr. MORE (*Regina City*): There would have to be differences. You then suggest that they should be given an opportunity to become chartered banks and yet not have the restrictions imposed on them in this field that the act will impose on the present chartered banks?

Mr. NEUFELD: Some of the restrictions, and one has to be explicit to make any kind of sense out of it. I think they should face the same restrictions with respect to inspection, control and supervision. I think they should face the same restrictions with respect to cash ratio requirements. I think they should face the same restrictions with respect to interlocking directorships and equity participation in other financial institutions; and so on.

The one area where one would have to make them different is in the character of their assets and in the character of their liabilities.

Mr. MORE (*Regina City*): You would make them different, as I see it, if I am right, in their operation; they could carry on operations they now carry on which the banks cannot carry on and would not be able to enter under the present proposals?



Mr. NEUFELD: The only case where this would be so is in the matter of fiduciary powers of the trust companies. The banks would be able to enter conventional mortgage lending under this bill?

Mr. MORE (*Regina City*): On a limited basis.

Mr. NEUFELD: Only with respect to residential mortgages; otherwise they are free to engage in conventional mortgage lending. They would be able to begin to build up their debenture business but on a gradual basis. These differences in fact are removed. The only thing left, really, is the matter of fiduciary powers and here I would say, as I mentioned before, that for a period of ten years I think the trust companies should continue to enjoy a monopoly in fiduciary powers, whether they are trust companies with bank charters or without bank charters.

Mr. MORE (*Regina City*): In an answer to Mr. Clermont you indicated that in your mind the banks have not been progressive enough in the past, and you have some doubts that even with the change in legislation they would be as progressive as you would like to see them. In what fields have they lacked this progressiveness? We have many instances of their being progressive enough to circumvent the act, as some people seem to call it, so that they can serve the public better. I am just wondering in what field you think they have lacked progressiveness?

Mr. NEUFELD: I think that is a very good question in the sense that it clearly illustrates that this can only be an impression and one cannot quantify this kind of viewpoint. What can one point to?

The CHAIRMAN: The matter of hours.

Mr. NEUFELD: I think that the matter of hours is an obvious one. I think that the banks have not done what they could to compete for the deposits of the smaller saver. I suggest the minimum quarterly balance rate of interest for everybody. The difference between a person who puts money in for three months and a person who keeps all his money in for twenty years does not to me make too much sense. It is this kind of aspect of the operation that I think lacks imagination. I sometimes also wonder whether they have been fully competitive in getting their share of the university trained people. Again this is just a subjective view which is not based on any analysis of the character of their employees but it is simply another general impression that I have.

Mr. MORE (*Regina City*): You mean that you think they have kept their wages too low?

Mr. NEUFELD: No, I would not say that they have kept their wages too low. I am wondering whether they should not be getting more of the kind of people that they could pay more wages to quite legitimately.

Mr. MORE (*Regina City*): You do not think there has been a change in that attitude in recent years?

Mr. NEUFELD: I think there has been a change. Unquestionably there has been a change. There is always change in the dynamic world. It is a question of how fast the change is.

Mr. MORE (*Regina City*): Apparently you do not agree with the banks' position, as the evidence given here has outlined, that there is an operating

account basis apart altogether from the loaning operation that must be charged and will continue to be charged—

The CHAIRMAN: Mr. More, if I could interrupt here. I think we are getting into the interest rate question which is the next topic. Mr. Wahn.

*(Translation)*

Mr. CLERMONT: Would Mr. Wahn let me put a question supplementary to the reply that the Professor has just put about university graduates?

The CHAIRMAN: It depends on Mr. Wahn, if he will agree to your putting a question.

Mr. CLERMONT: Professor would you not say the banks have had success with career officers? I remember one banking institution, 20 years ago, which had attempted to interest university graduates but some of these were not interested in beginning at the bottom. That was the problem.

*(English)*

The CHAIRMAN: So this will be recorded, Dr. Neufeld, the question is to note that our proceedings are being recorded electronically on tape and from there the verbatim proceedings are produced, so I think it would be more useful to the Committee if your replies were verbal rather than—

*(Translation)*

Mr. CLERMONT: The answer the Professor gave to Mr. More's question was also recorded, was it not?

The CHAIRMAN: I believe so, if it is an oral answer.

*(English)*

Mr. NEUFELD: From now on I will certainly say yes or no, as the case may be, instead of shaking my head.

In answer to your question, I really do not see any reason why formally trained people should start at the bottom in the sense of remaining at the bottom as long as others if they qualify as bankers, but I have to make clear that I am talking in an area in which I am no specialist at all. I do not know how fast they should push university students, or whether or not university students are a good thing in banking in general. I think they are a good thing.

*(Translation)*

Mr. CLERMONT: But with trained—

The CHAIRMAN: Mr. Clermont, I believe we are now entering a discussion—

Mr. CLERMONT: I am sorry Mr. Chairman, but I believe the Professor started discussing this subject.

The CHAIRMAN: Maybe it is my mistake, as Chairman, allowing the Professor to enter this field. There is a difference between dialogue and supplementary questions.

Mr. CLERMONT: I believe there is no objection, Mr. Chairman, when you ask supplementary questions yourself without asking the person who has the floor to ask these questions.

The CHAIRMAN: Maybe you are right, Mr. Clermont. Mr. Wahn, will you allow Mr. Clermont to ask his question?

Mr. CLERMONT: No, no, that is all right, Mr. Wahn.

(English)

Mr. WAHN: In the first section of your brief you indicate that you attribute importance to the fact that the banks are to be permitted to issue debentures. At the present time the banks issue what they call deposit receipts, which are somewhat similar to debentures. It is hard, from a legal point of view, to distinguish between deposit receipts and debentures. I do not know to what extent they do that, but if they have this power now of issuing what are essentially debentures, why do you attribute importance to this particular provision?

Mr. NEUFELD: Not being trained in the law I cannot give you a legal distinction between deposit receipts and debentures. I do think that the issue of debentures of the kind outlined in the bank bill I will appeal to the smaller investor, whereas deposit receipts do not because of their large denomination.

Mr. WAHN: You recommend, Dr. Neufeld, that the Bank Act be amended to permit trust companies and loan companies to become banks. It is a very interesting suggestion and very helpful, I think. Do you attribute great importance to this?

Mr. NEUFELD: Of all the items in the brief I would think it is by far and away the most important item.

Mr. WAHN: What is the reason you feel it is so important? Is it because you feel that greater competition is necessary, or is there some other reason?

Mr. NEUFELD: There are three or four reasons. I think the increased competition that it would generate would be a very good thing.

Secondly, I think that it would better enable non-banking institutions to meet the kind of competition that they are likely to get from the banks as a result of the amendment of the Bank Act.

I also think that it would improve the kind of financial services in this country available to the smaller saver and smaller investor. I think it would lead to a generally more efficient financial system. This matter of introducing changes that will permit financial institutions to evolve over time is an important one because I can point out instances in the past where existing financial institutions have not been able to evolve. It is not beyond the realm of possibility that in the absence of such changes some non-banking institutions will not be able to survive over time. I am not thinking about tomorrow; I am thinking over the long term of 10 or 20 years.

Mr. WAHN: At the present time chartered banks can only be incorporated by parliament. I believe there was some suggestion that this power might be taken away from parliament and given to the governor in council, but I believe at the present time the thinking is that they will continue to be incorporated only by parliament. If your suggestion is adopted it would mean a very great departure from this particular principle.



At the present time under our parliamentary procedure, as you probably know, chartered banks and, indeed, any other institutions which require to be incorporated by parliament must have bills which are passed in private members' hour, and it is possible under existing procedures for one or two members to refuse incorporation even to the most responsible institutions and people if they wish to do so. Have you given any thought or do you have any views as to whether or not under parliament's existing rules the incorporation of banks should be left exclusively in the hands of parliament?

Mr. NEUFELD: Again I must declare myself as not being an expert in parliamentary procedure. I would simply say that I cannot understand why anyone would think that there are advantages to be gained by slowing the process of granting bank charters. It seems to me the important thing is that certain standards be met and when an institution meets those standards then there should be no other delay in its obtaining a charter.

Mr. WAHN: Dr. Neufeld, you said earlier in response to a question that financial institutions have to be large in order to be efficient, and therefore you preferred to have legislation make it possible for trust and loan companies to become banks rather than for new banks to be incorporated. However, would you agree that it is also desirable that the incorporation of new banks should be facilitated and not unduly prevented?

Mr. NEUFELD: Yes, I have pondered over this because if you follow the logic of my argument you might say, "Well, let us concentrate entirely on permitting existing institutions to evolve and forget about the entry of new institutions". That does not really appeal to me very much. I think there should always be relative ease of entry into the industry.

In the financial industry this is particularly difficult because when they go bankrupt it is a serious matter for people who have left their savings in these banks. It was because of all these considerations that I did not confine myself to an approach that would permit existing institutions to evolve, but also to one that would make it easier for new ones to be formed, and this relates to my supporting the introduction of deposit insurance.

Mr. WAHN: Thank you very much, Mr. Chairman.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Could I ask a supplementary? I wonder, Dr. Neufeld, in connection with the questions Mr. Wahn has been asking about the relative desirability of having new banks chartered by the present process of the introduction of a private bill, or by a speedier method, if it is not due to the fact that one application we have had for a bank charter was held up by a number of us in the House of Commons, and eventually the people who were promoting this went bankrupt. There was a terrific row and it was a very good thing we did not incorporate it.

Mr. NEUFELD: Well, my only answer would be that I hope that the reason for your delay was that you were not content that they were meeting minimum standards.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The reason for the delay was that we had some doubts about the people who were promoting it.

Mr. NEUFELD: Well, I would include that in the matter of minimum standards.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You will agree that there are and will be occasions when a more deliberate scrutiny of proposers of bank charters is perhaps needed than the mere examination of their books and the issuance of a charter?

Mr. NEUFELD: I would certainly agree that in the case of some proposals they should be delayed indefinitely.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): That was our view in this case.

Mr. FULTON: Well, now, Mr. Cameron, I do not know—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The Laurentide Finance Company got into serious difficulties and the bill was withdrawn.

The CHAIRMAN: They did not go bankrupt.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No, they did not go bankrupt but they got into very serious difficulties. A great many people lost money.

Mr. LIND: But not in Laurentide.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): In Laurentide.

Mr. NEUFELD: Shareholders only, I think.

The CHAIRMAN: You are talking about the value—

Mr. LIND: The value of stock goes up and down. I think you should clarify your remark, Mr. Cameron. Laurentide, as I understand it, did not fail or—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): There were considerable losses. I know of one lady who is closely connected with one of the promoters of Laurentide. She was very annoyed that she had dropped a very large packet of money over this deal.

The CHAIRMAN: The loss was with respect to the value of her shares.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes.

The CHAIRMAN: There was nobody in the—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): They got into serious financial difficulties and then were taken over.

The CHAIRMAN: Was there anybody in the class of a depositor or holder of a debenture who lost money?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No, I do not think there was.

Mr. FULTON: In several of your answers this morning, Dr. Neufeld, as I appreciate it, you seem to have attached very much more importance in connection with your suggestion about trust and loan companies being allowed to become banks and much more importance to the economic advantage than to the advantage that might result from control and inspection. Have I interpreted you correctly?

Mr. NEUFELD: Yes, I think that on the whole I have emphasized the economic advantages although I have not ignored the other advantages, at least not in my own mind.

Mr. FULTON: Could you let us know if you regard that as important or only incidental, this factor of control and inspection? Is it an advantage in itself or is it just to you an incidental something which accrues?

Mr. NEUFELD: I think it is an advantage because it would mean that a larger proportion of the financial system would be under the scrutiny of the Inspector General of Banks. I think from the point of view of supervision that would be an advantage although I would wish to emphasize that this is not the advantage I see as being the crucial one in recommending the approach that I take, but it is an advantage.

Mr. FULTON: Am I right in saying that your proposal would not bring what I think can probably be categorized as the finance companies under the Bank Act, or under a bank type inspection?

Mr. NEUFELD: This would depend on the explicit kinds of financial standards and character that such institutions would have to meet or possess. I would say that it is my personal opinion that it would be most unlikely that the finance companies under present conditions would qualify. At the same time it is not inconceivable that one or two of them might qualify in terms of the way they might evolve over the next 10 or 20 years.

Mr. FULTON: At the present time hardly any, if any, would be brought under by adopting your suggestion?

Mr. NEUFELD: That would be my thinking.

Mr. FULTON: Speaking of the finance companies. Could you give us an opinion, I do not mean mathematically, as to the relative importance of the finance company in the field of money and credit?

Mr. NEUFELD: The finance company experienced a very substantial rate of growth from the end of the second world war until about 1957 or so and from then on, in terms of their relative growth, they have declined in importance. Therefore I think that their future importance will not increase, it will diminish.

From the point of view of the impact of their policies, actions and lending practices on the economy generally over the postwar period, I would accept the view expressed by the Royal Commission on Banking and Finance, which made a fairly thorough study of the matter. I think there were one or two instances in the postwar period when the credit that they granted probably acted in a destabilizing way, but there were very special reasons why that was so. My feeling now is that finance companies do not cause any serious difficulty for the monetary control authorities. Therefore, on those grounds one should not worry about the fact that they would be operating outside the Bank Act.

Mr. FULTON: My concern is not only that they are operating outside the Bank Act but they are operating outside the field of control and inspection at, if you like, the federal level.

Mr. NEUFELD: I agree, and I think the fact that as such there has not been separate legislation designed specifically for finance companies has probably been one of the reasons why they have escaped the kind of control that should



have been imposed on them. Not control for purposes of achieving economic objectives, but simply control for purposes of ensuring that savers do not lose all their money.

Mr. FULTON: Right. That, I think you told me, you do regard as an important objective?

Mr. NEUFELD: Yes.

Mr. FULTON: Then, since I think we are agreed that neither the present bank bill nor your proposal, if adopted, would attract them under this umbrella, it follows, does it not, that some other device from either of these two would have to be used?

Mr. NEUFELD: Yes. For example, if one changed legislation so that federally registered finance companies should come under the general supervision of the Superintendent of Insurance, that would be one approach.

Mr. FULTON: That would cover federally incorporated companies but, as in the case of deposit insurance which you support, you think it is at least an incidental advantage that non-federal companies may be attracted under it?

Mr. NEUFELD: Yes, it is an incidental advantage.

Mr. FULTON: Yes. Would you not agree, then, that it would be desirable if we could find some device that would attract non-federally incorporated finance companies under the umbrella of control and inspection?

Mr. NEUFELD: Well, this assumes that the provinces will not develop sufficient control procedures. I would not want to say that one need necessarily accept that assumption. I think there is evidence that the provinces are becoming quite concerned over the quality of their own inspection.

Mr. FULTON: Would it not be desirable, though, from the point of view of their impact in the field of money and credit, even though it would be diminishing, to have a uniform system of control and regulation?

Mr. NEUFELD: Oh, I do not know whether I like the word uniform. Control, I think, has to depend on the character of the operations of institutions, and if there are some basic differences in the way companies go about their business in the kind of control and supervision to which they are subjected it might well have to differ one from another. I do not really see any inherent advantages in having one supervisor controlling all financial institutions in general. It may well be that if you had one you would have to have separate departments dealing with different financial institutions in any case because their operations might differ quite substantially one from another.

Mr. FULTON: In the course of your evidence you answered a question earlier which I did not follow clearly. As I recall it, in some way you suggested that finance companies would be made sound, and I did not get at all how you felt they could be made sound without bringing them under the Bank Act or a system of regulation and inspection.

Mr. NEUFELD: I may be mistaken. If I said that finance companies would be made sound, I do not recall that I said it. I do not know within what context I said that. I do not specifically discuss finance companies. Certainly I do not see how any of the charges that I have suggested would lead to an improvement in

the financial position of finance companies. I think it is a quite separate matter. If finance companies began to take deposits they presumably would fall under the deposit insurance and inspection that that involves and it would lead to that. I may have forgotten that I said that, but I do not recall that I said that any of my changes would lead to sounder finance companies.

Mr. FULTON: Thank you. What is your opinion of the suggestion that finance companies be attracted under this umbrella, and also that they be made sounder by the device of the lender of last resort being extended to them under the federal aegis?

Mr. NEUFELD: I am not much attracted by that suggestion. I think that there is merit in imposing fairly high standards on any institutions that have the privilege of calling themselves banks. At the same time, I see great disadvantages in imposing such rigid standards on all institutions because I think it would destroy innovation in the capital market. This is one great disadvantage I see in putting everybody under one umbrella, and I always prefer to see a number of institutions that can operate with a fair degree of freedom and with minimal protection for the people that are involved.

Mr. FULTON: Can you rationalize that with the other assumption that it is desirable and essential that there be federal control over the monetary system?

Mr. NEUFELD: Oh yes, I think so, because in my view the kind of control that the federal authorities can exercise, control in the monetary control sense, through the central bank is pretty effective in that one does not need to bring institutions under the umbrella of the Bank Act for that reason.

Mr. FULTON: No, not the Bank Act. I do not mean to make them all banks. I mean a comparable system of inspection and control so that you have the organization of your financial system covered, although not necessarily within the same rigid pattern, but you do have a system and varying degrees of rigidity and adaptability, but under that whole system you have the whole of the financial organization.

Mr. NEUFELD: I think all financial institutions should be inspected. I do not think it is necessary to impose the same kind of inspection on all financial institutions.

Mr. FULTON: Well no, because now we have the insurance companies under one department and the banks and, if your proposal were adopted, the trust companies would be under another.

Mr. NEUFELD: If one is worried simply about the matter of providing minimum inspection of finance companies, to be specific, I think it would be quite appropriate to have a special finance company act which would outline the nature of that supervision and control and I would see no reason why, for example, the Superintendent of Insurance could not administer the act.

Mr. FULTON: But you would not want to see this part of the Bank Act. That is your point.

Mr. NEUFELD: I would not want to see it as part of the Bank Act.

You mentioned before the matter of providing lender of last resort facilities to these non-bank institutions. I would like to say that in general I support that

view. Under present arrangements the provision of lender of last resort facilities to non-banking institutions is on a very haphazard basis.

You will recall that in the case of British Mortgage and Trust it was almost by accident that the government of Ontario promised that it would, if necessary, deposit funds with British Mortgage and Trust, but the very announcement that it was prepared to do this was enough to restore a degree of confidence in the institution. There was a clear case of where the provision of lender of last resort facilities served an exceedingly good purpose and when the issue arises, and such facilities need not come from the Bank of Canada, they can be provided by others as in a sense Central Housing and Mortgage does in a way, but on principle I would say when the question arises one should view very favourable the matter of providing machinery for extending lender of last resort facilities to non-bank institutions.

Mr. FULTON: This would have, would it not, two obvious results; one, increase in stability directly and, two, increase in stability as a result of bringing them under an inspection and regulation system?

Mr. NEUFELD: Right.

The CHAIRMAN: Mr. Fulton, I wonder if we would not find it more convenient to continue in this afternoon's session. Mr. Latulippe has some questions.

Mr. FULTON: I have one or two more questions, if I may, this afternoon.

The CHAIRMAN: Yes, and we will continue with Dr. Neufeld and when we have finished our discussion with him we will proceed with Dr. Ziegel, whom I believe is taking the noon train from Montreal.

*(Translation)*

The meeting is adjourned until 3.45 p.m. this afternoon.

#### AFTERNOON SITTING

*(English)*

The CHAIRMAN: Gentlemen, we will resume our meeting. When we recessed for lunch Mr. Fulton had the floor and I recognize him again at this time.

Mr. CLERMONT: Mr. Chairman, is it your intention that this Committee sit next week?

The CHAIRMAN: Yes. We already have dealt with the report from the Steering Committee, which suggested that if the House met next Tuesday we would hear witnesses on that day. Do you have any suggestion about this?

Mr. CLERMONT: I can express only my opinion; I cannot express the opinion of other members of this Committee. I think possibly you may have some difficulty in making up a quorum. Personally I would prefer that we do not sit next week.

The CHAIRMAN: Perhaps we can give the matter further consideration later today. We already have agreed to hear Dr. Caterina and the Canadian Credit Men's Association on Tuesday, assuming the House meets on that day, but we always can reconsider a topic of this nature. Perhaps we might bear your comments in mind as the day continues, and then this evening we might return



to it to see whether or not we want to reconsider in light of the schedule of the House for next week. Mr. Fulton, I believe you have some further questions.

Mr. FULTON: Thank you, Mr. Chairman. Dr. Neufeld, I take it to be clear from your submission that you favour a melding of the types of business now carried on by the banks, on the one hand, and by the trust companies, on the other hand. You would like to see a melding of the two types of business. I do not mean amalgamations or mergers; I mean the two which are now separate, drawing closer with regard to the general nature of their activities?

Mr. NEUFELD: Yes, I would say that this melding together in fact, has taken place; I would say that recent legislative changes or proposals will encourage this trend and, finally, I agree with what is going on.

Mr. FULTON: Your brief also seems to contemplate that if your proposal were adopted then at the time of the next revision, in approximately 10 years, we should be prepared to consider—I do not know whether you go so far as to make a definite proposal now—letting the banks go into a fiduciary side of the trust business.

Mr. NEUFELD: Yes, that is right.

Mr. FULTON: Would this not bring about a situation where in fact you had a whole lot of new banks and at least eight new trust companies?

Mr. NEUFELD: Of course it will be recalled that the Canadian trust company is, in many respects, a unique institution. There is no parallel of it in the United States or the United Kingdom, where the banks have trust departments, so I would think that in time the larger institutions would develop trust departments. However, because the nature of the trust business, I think it would take a very long time for each individual bank to develop a large trust department. I would think that even with complete freedom, particularly if existing trust companies had, by then, become banks, they would continue to be a major factor in the trust business.

Mr. FULTON: If this trend were to take place, and to be encouraged or permitted by legislation, what legislative and administrative changes do you envisage as desirable to accommodate it, apart from the amendment of legislation. I am thinking of the fact the trust and loan companies are now administered under the act, and the supervision is administered by the superintendent of insurance. What implications in that field do you see?

Mr. NEUFELD: I do not think the implications there are very widespread. I really think that the major change would be the one of defining specifically the conditions under which such institutions would be granted charters. As far as the institutions that would not want to have charters, the legislation under which they operate and the supervision to which they are subjected is concerned, I would not think that on the federal level there would be very many changes, although I think one should look objectively at the possibility that such institutions be permitted to make commercial loans, which they are not now permitted to do.

Mr. FULTON: Would you see them coming under the supervision of the Inspector General of Banks and the supervision—if that is the right word—to whatever extent it is, of the Bank of Canada?

Mr. NEUFELD: No, I do not think that is necessary. I think there is no reason the superintendent of insurance—and one might give him a different title—would not be able to effectively supervise and regulate non-bank institutions.

Mr. FULTON: They would now be banks.

Mr. NEUFELD: No; we are talking about those institutions that would not apply for bank charters and would continue to operate under trust company legislation.

Mr. FULTON: No. I was envisaging that as a result of the legislative changes that you contemplate, the objective which you think is desirable is largely achieved and you have a number of new institutions not now engaged in the banking business but which would be engaged in the banking business, if I may use the words in quotes "by definition"?

Mr. NEUFELD: I agree.

Mr. FULTON: What about the administrative changes to accommodate that situation?

Mr. NEUFELD: I think that the only administrative change which would be necessary is that the Inspector General of Banks would have to be given adequate staff to extend his supervision to those institutions that have now become banks. Apart from that, I see no really great administrative changes.

Mr. FULTON: These institutions then would have the same relationship with the Bank of Canada as the present chartered banks?

Mr. NEUFELD: Precisely.

Mr. FULTON: Returning to the question of deposit insurance—in the light of the evidence you have given so far—you have said, on the one hand, that you think it is desirable that legislative restrictions be eased so the banks can be more competitive with the trust and loan companies, and converse to that situation; as I appreciate your position is, it is desirable and healthy that trust and loan companies should be competitive with banks.

Mr. NEUFELD: Yes.

Mr. FULTON: Then with respect to deposit insurance, is it your opinion that the scheme of federal deposit insurance is not necessary with respect to the banks from the point of view only of ensuring their stability?

Mr. NEUFELD: I do not think deposit insurance is necessary from the point of view of the banks that now exist and are now in operation. That is simply because the banking system in Canada is a very reliable one, and it is most unlikely that depositors would lose their money. This, in turn, is partly because of adequate supervision. On the other hand, it is my opinion that such deposit insurance would be desirable for some of the non-bank institutions and is desirable now for some non-bank institutions. It is really because of their position that I personally favour the introduction of deposit insurance.

Mr. FULTON: To that extent then, is it not correct to say that if the present chartered banks are compelled to come under the scheme of deposit insurance, it is being extended to them because it is desirable not with respect to any specific objective involving the banks but it is desirable for special objectives involving institutions which are not banks.

Mr. NEUFELD: That is precisely the case, and I think that in order to justify that sort of standard, one must remember that the banks have other advantages denied to non-bank institutions and that in a sense, their having to contribute to the deposit insurance scheme, might be seen to be a partial offset to the advantage that they now enjoy and that is denied other institutions. I am thinking specifically of their access to the lender of last resort facilities of the Bank of Canada, and to the tremendous advantage they enjoy by being able to call themselves banks.

Mr. FULTON: Yes.

The CHAIRMAN: Mr. Fulton, I hesitate to interrupt you this time but I understand from the Clerk that you have had approximately 25 minutes. If the committee is agreeable I certainly would permit you to complete your current two questions that you seem to be about to put.

Mr. FULTON: Thank you Mr. Chairman. I just observe though Professor Neufeld, that the banks also at the present time are under a restriction not applicable to these other institutions, and you are asking that the other institutions have the same privileges as the bank? I make this observation with respect to your last answer. My question follows. To that extent, therefore, does it not also follow the banks are going to be placed under a liability—an obligation they do not now have—to assume the obligation of participating in the deposit insurance scheme, whereas the trust and loan companies would not have to assume that obligation. Therefore, is it not in fact placing the bank in this respect at a fairly competitive disadvantage?

Mr. NEUFELD: I think this would partly depend on the rates that are finally decided by the deposit corporation, the rates that are actually paid. I do not deny the logic of your objection in a sense that one can argue that the banks would seem to be able to get along fairly well without it, and that if they are apt to participate in it, therefore, this would place them at a disadvantage that they would not labour under without the insurance scheme. I think that the logic of your argument is one that I must accept. But to get back to the other point, it is not all that bad because these banks do have certain advantages, conferred upon them essentially by parliament, I might add, in their relationships with the Bank of Canada, in that there are offsets to this disability that they operate under. And I must also go on to say that new non-bank institutions that would apply for and receive bank charters, would operate under the same deposit insurance regulations as the existing banks. So there would be no discrimination in advance of the new institutions, not having to meet the same requirements.

Mr. FULTON: Not as they become banks?

Mr. NEUFELD: Not as they become banks.

Mr. FULTON: In your view, could the successful operation of the deposit insurance scheme be doomed to failure if it was left to the banks to join or not, at their option?

Mr. NEUFELD: No, I would not necessarily say that it would be doomed to failure; indeed I would be inclined to think that it might be a good idea to begin as a purely voluntary scheme and see what happens, and then if it is not working out too well, reconsider. I am not at all sure that it might not work by having it a



completely voluntary scheme, including it being voluntary for the banks. I think only time would really tell whether or not it would work.

Mr. FULTON: We have been in the habit of amending the Bank Act only once every 10 years or in this case 12 or 13 years. Do you see any compelling reason we should not make isolated amendments to take care of particular situations more frequently than every 10 years. In other words, regard the Bank Act and its amendment as more flexible perhaps, with a more flexible approach than we have had in the past. In that way you could try these schemes, as you have just suggested, and change them if the weakness becomes apparent.

Mr. NEUFELD: Yes, I think so. However I think that the tradition of a decennial revision of the Bank Act is itself one that is worth while perpetuating because it insures that one has a comprehensive review of the banking system.

Mr. FULTON: I am not suggesting that we forgo this; I was suggesting that perhaps we might be more flexible in our approach and not wait for the decennial wholesale revision before we can attempt even individual amendments.

Mr. NEUFELD: I quite agree; I see no inherent justification for waiting 10 years to deal with important matters in banking. Some of the individual changes I foresee might well require a look after 5 years rather than 10 years.

Mr. FULTON: Thank you, Mr. Chairman.

Mr. LEBOE: Mr. Chairman, could I ask a supplementary question? It is related directly to the question that Mr. Fulton asked. He mentioned access to the Bank of Canada funds as one advantage, and the name of the bank as another advantage for the bank. Would you not include the fact that when a bank makes loans on many occasions it also creates a deposit with that same bank? I am really thinking of a system, not an individual bank.

Mr. NEUFELD: No. The only way in which that can be regarded as an advantage is that people have come to regard a bank deposit as being something that is so reliable that they can use it as money. This is not an advantage conferred on banks by any government; this is something that the bank deposit has acquired because the banks, over the years have carried on their business in a reasonably efficient and confident manner. So I do not think that it is right to regard their ability to have their deposit liabilities used as money, as something conferred on them.

Mr. LEBOE: The reason I asked that question is that we have evidence here that the trust companies also do the same thing.

Mr. NEUFELD: That is right.

Mr. LEBOE: I put my question that way to get a particular answer.

The CHAIRMAN: Thank you, Mr. Leboe.

(Translation)

I give the floor to Mr. Latulippe, and I trust that we have an interpreter in the booth, can you hear? Mr. Latulippe, have you some questions?

Mr. LATULIPPE: I have some questions, and my questions are on the character of obligations. My first question will be put to the Professor. Why are

holdings of Caisses Populaires near-banks or trust company not part of the money supply?

The CHAIRMAN: Mr. Latulippe, I regret to interrupt you, but we are now discussing the question of setting up banking institutions, federally speaking, and of making a group of near-banks into federal institutions. We are not now discussing obligations in general or the money supply. When we come to bank reserves, you might put your questions again, under that heading, that is under items 4 and 5 in the statement of our witness.

Mr. LATULIPPE: Mr. Chairman, it seems the question has a relationship with the near-banks. There has been some discussion of near-banks.

The CHAIRMAN: But we are speaking of near-banks in a certain sense, are we not? We are discussing the methods, the needs, the need to bring near-banks under federal jurisdiction and how we are going to go about it.

Mr. LATULIPPE: If you will allow me, I have no objection to waiting to put these questions again. I will yield the floor to someone else.

The CHAIRMAN: I have put the same request to some other colleagues.

(English)

Are there any members who have not had an initial opportunity to question our witness on the question of banking legislation, non-bank institutions and deposit insurance? If not, I would suggest that we move on.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Chairman, before we move on, may I ask one final question on this?

The CHAIRMAN: Yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Dr. Neufeld, just so that we can wrap this proposition of yours up, I gather that you envisage these trust companies which are to become banks as performing all the functions of banks plus their judiciary functions, at least for the next 10 years, as distinct from the chartered banks.

Mr. NEUFELD: That is right sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): What is your view as to the provisions for cash reserves which govern the banks. Will they govern these new banks?

Mr. NEUFELD: I would think that the cash reserves that apply to these new banks should be identical to the cash reserve requirements of the existing banks.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): In answer to a question, I think of Mr. Fulton you said that you would consider that they would be able to move into the field of commercial loans.

Mr. NEUFELD: Yes, I would expect that they should.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): And would you consider that the same interest ceiling provisions which will prevail for some time at least after the passing of this act should apply to them too?

Mr. NEUFELD: They should apply to the commercial lending business of those new banks, yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Thank you that is all.

Mr. FULTON: Are we going into these categories of chartered banks, near-banks and instant-banks?

The CHAIRMAN: I would suggest to the committee that we move on to the major topic raised by Professor Neufeld, the question of the interest rate ceiling on bank loans. I suggest, as we agreed this morning, that we combine with that the topic of the proposed interest rate disclosure provision. I suggest to the committee that it would be in order to refer to Professor Neufeld's preliminary discussion of these topics in the introductory portion of his brief—and I yield the floor to Mr. Clermont.

*(Translation)*

Mr. CLERMONT: Mr. Chairman, before I put some questions to Professor Neufeld, when the Committee receives briefs which are only in English, could not the Committee circulate a French version to the French-speaking members?

The CHAIRMAN: You know, Mr. Clermont, that it is the goal all to committee—I am informed that she has asked for the translation of the unilingual briefs and the Bureau for Translations is working on this but it is rather slow about these things. It is a very serious problem, a problem we will have to solve. The clerk indicates that she attempted to get a translation ready for us to-day. I am certain that you will be in agreement with me when I say I would be rather difficult to ask an individual witness whether he be French or English speaking to attempt to have a translation from his own resources.

Mr. CLERMONT: You have noticed, Mr. Chairman, in my remarks I said when a brief is submitted in a language, "could the Committee", is what I said. I did not say it should; I said, could the Committee take it upon itself to circulate?

The CHAIRMAN: Oh, yes. I think this is our duty. It comes within the authority of the Committee. The clerk says she asked for a full translation from the Bureau for Translations at the Secretary of State Department, and it is a pity that we have not got the translation at hand already. And I will make every effort to see that the same be not true of statements coming in future. Thank you. I would thank you for having pointed out this shortcoming.

Mr. CLERMONT: Professor Neufeld, with regard to the ceiling on interest rates, in your brief, page 6, it seems that you would favour the abolition of the ceiling on interest rates that on a scaled period, not immediately, but in stages as proposed in Bill C-222, clause 89. If the section were adopted as in that bill, do you have any idea how much time it would be before the ceiling would be reached?

*(English)*

Mr. NEUFELD: I think that because present indications are that economic conditions are going to remain fairly boyant, if not quite as hectic as they have been, it is quite conceivable that interest rates would be such that there would be no removal of the ceiling for an indefinite period. Now there is not too much point in saying it will be three years, five years, or ten years, because such an opinion must be based on an economic forecast and economic forecasting is still a very hazardous business.

My own personal opinion would be that the provisions of the existing bill are such that it would be quite a long while before the interest ceiling would be removed.

*(Translation)*

Mr. CLERMONT: Basing myself on your report, could you explain your second reason that the ceiling might be eliminated abruptly? You suggest  $\frac{1}{2}$  of



one percent a year over a five-year period, and that would mean that from now on up to 1972 the interest rate would be  $8\frac{1}{2}$  per cent. But if Bill C-222 is adopted by the House of Commons, the rate would be  $7\frac{3}{4}$  percent for an indefinite period. But you claim it would be a number of years. Other witnesses said it will not be before three or four years. Others claim it would not even be during the next decade while the present revision is in effect. Could you give us an explanation—

(English)

Secondly, it will bring an abrupt end to the ceiling. As I explained earlier, a more gradual but complete move would be desirable.

Mr. NEUFELD: Well, I think that the major point that I had in mind, when I came to that conclusion, was that an abrupt removal of the ceiling, whether it takes place two years from now under the existing formula, or immediately, as some recommend, might lead to undesirable repercussions both in terms of their effect on non-bank institutions, and in terms of their effect on some borrowers. I think it will take time for borrowers to readjust themselves to a condition under which bank interest rates are completely free, interest rates, as far as the effect on non-bank lenders are concerned, one can only speculate, but I think that it is conceivable that there might be undesirable repercussions there as well.

I have in mind particularly the apparent effect in the United States under recent changes of the increase in the rate that commercial banks there pay on savings deposits and the effect of that increase on their savings and loan associations. As far as one can tell, there was a very substantial flow of money out of the savings and loan associations when the commercial banks in the United States increased sharply the amount that they paid for savings deposits. And some of the savings and loan associations, because of this I think, encountered financial difficulty. So simply to ease this transition both for the non-bank institutions and for people who borrow from banks it was thought it should be a gradual process.

Now, the other point is that I think it should start immediately because I think it is in prosperous times that both borrowers and non-bank institutions can make the necessary adjustment. The trouble is that if you do this when interest rates are low that is also the time when business is not so good and when profits are not so boyant, and the readjustment that is necessary, I think, would be more difficult when interest rates are low than when they are high.

Mr. CLERMONT: Do you think that if business is in a kind of a slump that the interest rate ceiling will establish itself by competition?

Mr. NEUFELD: You mean that the ceiling will be removed?

Mr. CLERMONT: No. I mean that if business is slow and there is more money available to borrowers, the interest rate will be established by competition?

Mr. NEUFELD: Well I think it will tend to be that we are dealing here with not just a matter of the general level of interest rates, but one particular interest rate that applies to one particular type of institutions, namely the chartered banks. Certainly I agree with you that if economic conditions become somewhat soft, the competitive position of the bank is improved because of changes in the legislation under which they operate, and they will be in a position, even when

interest rates are low, to be more competitive, to offer more attractive rates, than they would have been before those legislative changes were introduced.

(Translation)

Mr. CLERMONT: If the interest rate were higher, would there not be big companies who, instead of borrowing from the banks, would go into the bond market?

(English)

Mr. NEUFELD: Yes, I would hope that they would. I think that many large companies have been using bank accommodation because they have been getting it as a fairly low price. As far as the banks are concerned, this is the type of business they want to do because under a ceiling, where you have to charge everybody the same rate, you are inclined to lend money, I think, to the safest borrower. So that if the ceiling is removed, I think this would mean that the bank loans would be too costly for some of the very large institutions or companies that have fairly easy access to the capital markets. This would free money would the banks could then use to lend to the smaller institutions, including the businesses that would want to take medium term loans under the new provisions that permit banks to make mortgage loans. So I think that the direction of the change that you suggested is the correct one, and I think it is a very desirable one.

(Translation)

Mr. CLERMONT: The interest rate should be known to the borrower. Would these be commercial loans, business loans, or consumer loans?

(English)

Mr. NEUFELD: I would favour interest rate disclosure legislation that encompasses all loans. I think banks should be required to indicate clearly the annual rate of interest that they charge on any loans that they make, whether these are business loans, personal unsecured loans, installment loans or mortgage loans.

Mr. LAFLAMME: Do you mean then that the service charges would be changed into interest rates?

Mr. NEUFELD: Yes, they should be because I think there is a great deal of misunderstanding about the nature of interest rate. Interest rate, to my mind, as it is used in this context, is simply the cost of money and nothing more. Therefore, it must include all charges, not just something that is arbitrarily defined as interest rate. Indeed, I will go so far as to say that where banks required compensating balances, that is an additional charge, and that should be part of interest rates.

Mr. LAFLAMME: So instead of saying 6 per cent plus, it should be 7 or 8, according to the terms.

Mr. NEUFELD: Exactly.

Mr. CLERMONT: With regard to the compensating balance, it seems that for you interest rate and compensating balance is the same thing. But as you are aware, the banks are asking compensating balances from customers who do not even borrow money.

The CHAIRMAN: I suppose that the professor is referring to cases where compensating balances are required from borrowers.

Mr. NEUFELD: Yes, I am referring to the case where, as a condition for receiving the loan, compensating balances be maintained.

Mr. CLERMONT: The banking association representative said that it was not so.

The CHAIRMAN: I think in fairness to the bankers, Mr. Clermont, they said that they called for balances in two cases which might be quite distinct: in one case where there may not be a loan, but an account is maintained in which there is a lot of activity, and the other case, where there is a loan in addition to an account.

Mr. CLERMONT: I did not think Mr. Chairman, that the question of compensating balance was a "must" to obtain a loan.

The CHAIRMAN: No, I do not think that they said it was a "must", but I think that many members of the committee put questions to indicate that in many cases where there were loans, these balances were requested.

Mr. KNOWLES: I do not think that they operated the account.

The CHAIRMAN: No, I do not think that it is relevant to that, although we can check the records and see. Perhaps other members of the committee may test their own memories. My recollection was that they indicated that there were two circumstances perhaps inter-related where the balances were required, one, in cases where there may not have been a loan but there was an account in which there was considerable activity, and they also admitted that there were cases where balances were required above working balances in accounts that were linked with loans. I am not saying in every case.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I think you are right. They did outline the two cases in which they called for compensating balances.

Mr. LEBOE: Mr. Chairman, is there not a third, where they actually make a monthly assessment? I know one borrower has informed me that he paid \$250 every month to the bank for carrying his account.

The CHAIRMAN: Well, we may have to ask the bankers back to go into this further. To make sure that there is no misunderstanding, I think that Dr. Neufeld was referring only to situations where a person who has borrowed money from the bank is asked to keep a compensating balance in addition to any rate of interest he pays.

Mr. CLERMONT: Mr. Chairman, that is why I want to come back to that. I was under the impression that the bank's superintendent told us that there was no question between a loan and administration of a bank account, and that a compensating balance was requested because so many cheques or transactions were issues during the month. I think Mr. Gilbert put that question at different times to the bankers association representative. Am I correct, Mr. Gilbert?

Mr. GILBERT: I think the Chairman has put the problem in its proper light, in setting forth the two categories.

The CHAIRMAN: We are hampered somewhat because of the slowness of the transcripts, but I think that it is clear that the bankers did agree with me, if not



with other members, when I suggested that while the bankers themselves may segregate the cost to the borrower into two areas, the interest paid on the loan and the charges which are charged against the deposit account made into which the proceeds of the loan are deposited and in which cheques are drawn, insofar as the borrower was concerned that was part of the total package that he had to assume to use the services in question to link with the loan he made. And the committee may recall that I brought to its attention the very term used by the Bankers Association itself when it made its presentation to the Porter Commission, when it referred to what is called—the cost of borrowing. At that time—and I can remember reading this into the record—the bankers association said that interest rates were preferable to compensating balances, which must mean that they considered that compensating balances in some cases could be the same thing as interest rates; then went on to say, as I recall it, that service charges were even more preferable when compared with compensating balances, which to me would imply that even service charges could be brought into an interest rate. We can read that for ourselves.

Mr. KNOWLES: Mr. Chairman, is it not also true that in answer to a rather direct question: "If the interest ceiling was raised or removed, would this do away with compensating balances and service charges?" The answer, as I recall it, was "No."

The CHAIRMAN: That is right.

Mr. KNOWLES: Without any qualification.

The CHAIRMAN: That is right. I just want to say, that in fairness to the banks, we might have to ask them back to find out whether, in that context, they were referring to activity in an account where there was not a loan or otherwise; We may want to keep that in mind.

Mr. ADDISON: I wanted to ask Professor Neufeld a question on this discussion.

The CHAIRMAN: Just a moment, we started with Mr. Clermont.

Mr. CLERMONT: I yield to Mr. Addison.

Mr. ADDISON: I gather, Professor Neufeld, you are suggesting in essence that we remove the clause from the Bank Act whereby banks are authorized to charge a service charge with the consent of the customer and incorporate a service charge in the interest rate?

Mr. NEUFELD: Yes, I think the banks should be permitted, in time, to make whatever charges they wish to make. All I would say is that since this is all part of the cost of borrowing money, and in cases where the service charges are a part of the cost of borrowing money, that should be part of the disclosed rate of interest. This is not to say that they are not service charges that have nothing to do with borrowing money. Those service charges that are clearly a part of borrowing money should become part of the interest rate that is clearly disclosed.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): May I ask a supplementary question with regard to service charges that are levied in respect of a loan account. You would then advocate that the service charge should be based on the activity in that account?

Mr. NEUFELD: It may well be that there would be a loan account that might all be drawn out, but it might also be drawn out bit by bit, to be quite accurate.

It might well be that the bank has a scale of charges, for example, for the amounts of the cheques drawn against an account, quite apart from the loan. This would apply to people who had no loan from the bank. I would see nothing wrong with that.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But in the case of a loan, you would have that charge included in the interest rate?

Mr. NEUFELD: Well, not necessarily this charge, but if the condition of the loan was, for example, that a man had to maintain a compensating balance then, rightly viewed, the cost of that compensating balance is part of the loan. But the very fact that a person takes a loan would mean that he would also have to pay whatever it is he pays for every cheque that is drawn against the account to which the proceeds of the loan were credited. That would not be necessarily be a part of the cost of the loan because it would even apply to people who had no loan from a bank.

(Translation)

The CHAIRMAN: I think we will come back to you.

Mr. CLERMONT: Mr. Chairman, I think the supplementary questions and replies given by the professor complete my questions in regard to the interest rate.

The CHAIRMAN: Thank you, Mr. Clermont.

(English)

Mr. LAMBERT: May I interject here? When you speak of a loan account you are talking about an asset item on the balance sheet, not the liability side, because there has been a horrible confusion from the opening day here as to the difference between a loan account and a deposit account. There is a clear distinction. It is quite readily understandable that a loan account is an asset item, and the deposit account, which is the bank's liability, is a liability item on the balance sheet. There has been a tremendous confusion, if I may say so, and therefore I think a good deal of the discussion with regard to compensating balances and service charges has unfortunately been related to a loan, and unless there is a clear understanding that when you are borrowing, say, \$6600 that \$6000 will be useable in a deposit account but \$600 must be reserved somewhere else, I do not think one can talk about compensating balances in regard to a loan account. One can talk about compensating balances with regard to a deposit account in lieu of service charges.

Mr. NEUFELD: Well, I have not been aware of any confusion. I think that—

Mr. LAMBERT: I beg to differ—

The CHAIRMAN: Order, please. I think we should allow Dr. Neufeld to continue his comment.

Mr. LAMBERT: You were confused in your terms this afternoon.

Mr. NEUFELD: I certainly agree with you that a liability is not an asset, but I do think that if an asset is created under conditions that affect the cost that

arises on the liability side, to be specific one can legitimately say—and really, I am only supporting your view here—that if a loan, which is an asset, is granted on condition that the liability that that creates involves maintaining minimum balances, then it is legitimate to regard the treatment of the liability as part of the cost of the loan.

Mr. LAMBERT: This does not take into account the activity of the account.

Mr. NEUFELD: That is quite another matter.

Mr. LAMBERT: Then how can you make the distinction when you come to a compensating balance as to whether it is held for service reasons or for, shall we say, an increase in the actual interest rate?

Mr. NEUFELD: Well I think the activity of the account is indicated by the number of debit items against the account. If the charge is based on the number of debit items, I do not think there is any problem as far as I can see.

Mr. LAMBERT: Then how can one put into any note, shall we say, or into any agreement that the true charge for this loan shall be so much if a substantial portion thereof is attributable to the servicing of the deposit account?

Mr. NEUFELD: I think the question you raise is one of the technical difficulties that might be encountered when one comes to define the interest charged or the cost of the loan. I think there are technical difficulties and I think the one you have mentioned is one, and there are others. At the same time, I feel that the advantages to be gained in telling a borrower more or less what the money is costing him are greater than the technical difficulties that are going to be encountered in arriving at a figure.

Mr. LAMBERT: Until you try to enforce that figure in court?

Mr. NEUFELD: That may be so. I think opinion has begun to swing to the side of it being possible to define interest costs in a way that permit institutions to state average annual rates of interest. I do not deny the technical difficulties involved.

Mr. LAMBERT: Thank you, Mr. Chairman. I am sorry if I intruded.

The CHAIRMAN: I was just about to recognize Mr. More and he did not object, so I assume that Mr. More found your interjection to be satisfactory.

Mr. MORE (*Regina City*): Well, I had not realized that Mr. Clermont had finished. I thought these were all supplementaries we were getting here.

The CHAIRMAN: It seems we are operating so much as a unit now that it is hard to tell where one train of thought begins and another leaves off. I guess that is the explanation.

Mr. MORE (*Regina City*): I think most of what I had in mind has been answered, although I am not clear from my recollection that there was ever an admission from bank witnesses at any time that compensating balances and additional charges were ever part of the cost of the loan. They were all having to do with an account, and that in effect a loan might well create more activity in an account which resulted in high higher charges, and there was reference to the question of whether the holder of the account wanted service charges or a compensating balance, and on that basis they determined the compensating balance.



The CHAIRMAN: I think you are quite right, Mr. More, in saying that they outlined that particular state of affairs, but it was my impression that they, in effect, admitted—perhaps a bit reluctantly—that there were other circumstances in which compensating balances were asked for and which had the effect of increasing the total cost to the borrower. You may recall my bringing to the attention of the committee the bankers association's own words in its submission to the Porter commission, which were, "Only when compensating balances are in excess of ordinary working balances would the cost of bank credit to borrowers be raised, but this can be achieved more simply through higher interest rates, which are to be preferred because they state precisely the cost to the borrower. To require compensating balances disguises the true cost of credit to the borrower." Now, this is what the bankers said to the Porter commission. They may have changed their minds since. If so, they are at liberty to tell us, but I am afraid they are fixed with these words.

Mr. LAMBERT: This was not testimony before us.

The CHAIRMAN: No. But we—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): They adopted it before us, as I recall. I think the Chairman asked them if they endorsed it and I think the witnesses said yes.

The CHAIRMAN: They are the words of the same group. We will have to assess the value of these words under the circumstances in which they were given. It may be that they treated the Porter commission less seriously than this committee, or perhaps they treated the Porter commission more seriously than this committee. We may want to inquire into this in due course.

Mr. NEUFELD: May I just record, Mr. Chairman, that my views are precisely those stated by the bankers in their brief to the Porter commission.

The CHAIRMAN: Mr. More, do you have a question?

Mr. MORE (*Regina City*): Professor Neufeld, with regard to your suggestion that interest rates should be raised in what seems to be the rather mechanical method of one half of one per cent annually rather than the present formula suggested in the new bill, you referred to the development in the United States. What was the change in rate that brought about the results you referred to?

Mr. NEUFELD: Well, the commercial banks were permitted to pay more for savings deposits. The control there is on the savings deposit side.

Mr. MORE (*Regina City*): What was the increase, one per cent, one half of one per cent?

Mr. NEUFELD: I will not give a figure because I am not certain of that figure, but part of the repercussions—there were other things happening at the time—seemed to have been that the increase was sufficient to attract money away from savings and loan associations into commercial banks.

Mr. MORE (*Regina City*): But you cannot give me the figure?

Mr. NEUFELD: I do not have the figure here.

Mr. MORE (*Regina City*): I wanted to see how it compared with your suggestion of one half of one per cent and what the repercussions of that to other institutions might be.

Mr. NEUFELD: Let me clarify the viewpoint. Their control was on the savings deposit rate. In Canada the control is on the loan rate and will continue to be on the loan rate, so that there is at least one inherent reason to believe that a one half of one per cent increase in the loan rate will result in a one half of one per cent increase in the savings deposit rate.

Mr. MORE (*Regina City*): Whatever increase it might result in is not sufficient, in your view, to create great jeopardy for other institutions?

Mr. NEUFELD: No, I do not think it would create jeopardy.

Mr. MORE (*Regina City*): And you think that a mechanical formula, without regard to changing conditions in the financial market in this period, is preferable to the suggestion contained in the present proposal?

Mr. NEUFELD: Yes, I think so because the present proposal, I think, has two weaknesses. First, depending on short term rates, it might indefinitely postpone the movement toward a free rate and, second, under the formula when the free rate comes it will come all at once.

Mr. MORE (*Regina City*): And it might come at a time when its effect on the market—

Mr. NEUFELD: Well it might come at a time, if it came all at once and if competitive conditions were of a certain nature, when it would have an unnecessarily sharp impact on the short run in other institutions.

Mr. MORE (*Regina City*): Do you think, in your view—and as you have said, it would require an economic study—that the formula suggested in this present bill would result in the freeing of the rate before the next revision of the Bank Act?

Mr. NEUFELD: This involves a long term economic forecast. I would say that it would only result in a freeing of the rate if the country moved into at least a minor recession. If we maintain present levels of prosperity, then I think there would be no freeing of the rate between now and the next Bank Act revision.

Mr. MORE (*Regina City*): You do not, then, agree with the views of the witness at our last sitting when he suggested that the fluctuation that takes place in the short term market is really not contained by the strength at the top of the market and there might be fluctuation in the short term market sufficient—even under these conditions—to bring about the freeing of the bank rate within, I think you said, perhaps five years?

Mr. NEUFELD: It is certainly true that short term rates fluctuate much more than long term rates. At the same time, they usually do so only when there is a recession. Therefore, even for short term rates to come down, it would require a distinct slowing down of economic activity.

Mr. MORE (*Regina City*): To go back to your formula, then, would the impact on the borrower not be that banks would tend to operate on six month notes, with a renewal at the next highest half per cent, rather than changing it on this mechanical force? Does it not mean that the banks might well change their operations so that they can take advantage of the scale coming up at the increase?

Mr. NEUFELD: I think most bank lending is essentially short term lending at any rate, and there would be a one year interval between changes.

Mr. MORE (*Regina City*): And that in effect it would not change present bank policies?

Mr. NEUFELD: I do not think so because most of the bank loans are short term loans now.

The CHAIRMAN: I will now recognize Mr. Flemming.

Mr. FLEMMING: Mr. Chairman, I was interested in Dr. Neufeld's recommendation at the bottom of page 4, where he recommends that:

...the 6 per cent ceiling be raised by  $\frac{1}{2}$  per cent per annum for five years—

He mentions that the considerations about making it gradual is part of the determining factor of the recommendation. Then he said that there are other considerations and this, I think, is the right language. I happen to favour this general policy of a gradual increase, but what I would like to know first of all, Mr. Neufeld, is what are the other considerations and then, secondly, do you not think that if it gets up to an  $8\frac{1}{2}$  per cent ceiling, which would be envisaged under your recommendation, that this ceiling would impose quite a hardship upon business in general?

Mr. NEUFELD: In answer to the first part of your question, the other considerations that I had in mind are the ones that are referred to on page 8, which were essentially that under the existing formula, it is conceivable that the freeing of the rate would be indefinitely postponed and that my formula would not indefinitely postpone the freeing of the rate. That is one other consideration. In addition to that, I had pointed out that the advantage of my approach is that it would not be an abrupt change, it would be a gradual change, which is desirable for permitting borrowers and other financial institutions to adjust themselves to the change. I have forgotten the last part of your question.

Mr. FLEMMING: The last part of the question was if at the expiration of the five year period the ceiling rate is established at  $8\frac{1}{2}$  per cent, do you not consider this would be a hardship on business in general?

Mr. NEUFELD: No, I do not think so. I think that it would help many businesses because it would enable those that now have to seek funds from nonbank sources at quite high rates of interest to obtain this money from the banks. Secondly, it would enable such businesses to take medium term loans from banks. This I suspect, if we look at the changes in the legislation five years from now, will be one of the most important things that has happened; that some small and medium sized businesses will be able to get conventional mortgage loans from the banks to expand the physical plant of their operations. I think it is a highly desirable trend that changes in the Bank Act will lead the banks into more conventional mortgage lending, and I think that freeing of the rate will make this possible.

Mr. FLEMMING: I presume when you say conventional mortgage lending you also include the ordinary term loan of, say, six to eight or even ten years?



Mr. NEUFELD: Yes, except that presumably that term loan would now be secured by property.

Mr. FLEMMING: We are, of course, interested in any change which is going to be beneficial to business and to the country in general, and in the light of the knowledge which you have gathered of the activities of banks in the United States, and the fact that they have no ceiling in operation, would you consider that the average interest rates charged to business by the U.S. banks is greater than that charged by the Canadian banks, speaking in broad general terms?

Mr. NEUFELD: The trouble is that the statistics necessary to give a really competent answer to that question simply are not available. In the United States there are substantial differences between regions in interest rates. In Canada the problem is that we have no bank interest rate information at all. We can assume that the rate of interest is 6 per cent, but this is not a reasonable assumption because there are loans made at other rates and there are service charges and there are compensating balances, and so on. It is my impression, but it can be nothing more than that, that the average cost of bank money is not very different between the two countries, principally because of the interest rate ceiling in Canada. I might say this has been a very recent change, because it has only been in the last year or two that interest rates have risen to almost historic levels in the United States. Generally, before that I think it was clear that interest rates were lower in the United States than in Canada. Right now I am not sure.

Mr. FLEMMING: We certainly go there to do a lot of borrowing, do we not, and I suppose this is partly due to the fact that more money is available. But it is also partly due to the fact the money is cheaper.

Mr. NEUFELD: If we are talking about the sort of borrowing Canadians do down there, I think there is no doubt that the American interest rates are  $\frac{3}{4}$  to 1 per cent lower than they are in Canada. That is, borrowing in the form of the sale of bond issues.

Mr. FLEMMING: Professor Neufeld, on what basis did you arrive at the formula of  $\frac{1}{2}$  per cent per year over the five year period?

Mr. NEUFELD: It seemed to me that to stretch out this transition over a five year period would give business and borrowers quite a lot of time to readjust their business in any way they want. In the end this must simply be a judgment.

Mr. FLEMMING: I recall at the time of the coming into operation of the Bank of Canada Act that all the banks were allowed the privilege of printing, if you like, a certain amount of money and this privilege was taken away but, as I recall it, it was taken away over a ten year period. It was reduced by 10 per cent, 20 per cent, 30 per cent, and so on, until it disappeared. I am wondering what your experience has been in an examination of this situation in the large centres of Canada during that transitional period. What was the effect on the banks? What was the effect on the public in general?

Mr. NEUFELD: The problem there was quite different because the banks were the only ones issuing notes and therefore whatever happened to them did not really affect any other institution.

Mr. FLEMMING: The reason for my question was the fact that it was made gradual at that time to, if you like, soften the blow as far as the banks were

concerned because they were losing the so-called free money, were they not, and they did lose it?

Mr. NEUFELD: Yes, it gave the banks time to so adjust the asset side of their balance sheet to accommodate the change that was occurring. There is no doubt about it that in 1934 when this began bank notes still formed a not insignificant part of the source of funds of the banking system, and if it had been abolished overnight it would have caused substantial disruption of the banking system. Therefore, as far as I can tell, the gradual evolution worked very well. It was actually in 1950 that the last chartered bank notes legally disappeared from circulation. It was a very long period and, as far as I can tell, this changeover was effected without any great problems. I do think that that was quite another problem because in that case one was really taking away quite an important source of funds from an institution and placing it in the hands of government.

Mr. FLEMMING: Mr. Neufeld, I think probably those are all the questions I have. I do not want to take the time of the Committee with further questions. I was particularly interested to ask you what your opinion was relative to the general effect on the business of the country if your recommendation should be adopted. Is it your opinion that it would be a gradual application of permission to apply a higher rate but not necessarily the application of the higher rate?

Mr. NEUFELD: That is quite right. That is how I would view it.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Professor Neufeld, I am inclined to agree with Mr. More that it is rather a mechanical one-half on one per cent per annum and I am just wondering if you do not think there might be a tendency, at least in the last quarter of each year, for banks to hold back a little bit on the lending of money until the next one-half of one per cent came in. I do not know. Do you think they might do this?

Mr. NEUFELD: I do not think so because I think if they treated their customers that way the customers would get very angry.

The CHAIRMAN: What could they do about it?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): There is not much you can do about it anyway except get angry.

Mr. NEUFELD: I would not agree. I think that the banks, as is the case of most competing institutions, have to be concerned with what their customers think.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I noticed, in answer to one of Mr. Flemming's questions, your answer suggested that you were under the impression that the ceiling on interest rates applied to lending on mortgages.

Mr. NEUFELD: No, the ceiling on interest rates would not apply to lending on mortgages.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You said that the releasing of it, whereby the banks could charge at the end of your five year period  $8\frac{1}{4}$  per cent, would enable them to get into the mortgage field more readily. Actually there is no limitation on the interest rate in this proposed legislation for mortgage lending on the part of the banks. I wonder if that might alter your view about the necessity of removing it altogether in five years?

Mr. NEUFELD: You are quite right that there is no limitation on the interest rate the banks will charge on mortgages, but the point I was trying to make was that if the bank lending rates rise, some of the big borrowers will no longer take their loans from the banks, which will free the banks to direct it to mortgage lending.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I see. What is your view, Professor Neufeld, of the possibility—and the value of it—of there being an agency to set a maximum rate of interest across the board?

Mr. NEUFELD: I think it would be very undesirable. I think the capital market is probably one of the most efficient markets we have in the sense that people do respond to price in the capital market. Therefore I think that price should be permitted to be flexible in this market so that capital can be allocated to the best places. At the same time, I would urge that any freeing of interest rate be accommodated by interest rate disclosure. Unless people know what they are paying the capital market cannot work well. The capital market cannot work well if one freezes rates, and it cannot work well if people do not know what they are paying. So I think both of those changes are in the same category. They should come together, because they would both make the capital market work more efficiently.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I gather from an answer that you gave to an earlier question—as you say, they work together—you would not favour the lifting of the interest rate ceiling unless there was this disclosure.

Mr. NEUFELD: Yes, that is right, because I do not see the point of increasing the efficiency of a capital market in one way, which at the same time reduces its efficiency in another way. So that if one freed the interest rate to permit the banks to charge anything but at the same time permitted them not to say what, in fact, they are charging, then we would introduce another obstacle to the efficient functioning of the capital market. Therefore I would argue that they should go together, and if they do not go together there should be no change.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then you would advocate the inclusion in this legislation of a definition of charges for loans, not necessarily interest. I suppose you would put it in those terms.

Mr. NEUFELD: Yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): How would one go about doing that?

Mr. NEUFELD: I have read a great deal about the complexities of determining the cost of money. It is a highly technical problem. I am convinced that since the main purpose of this is to give a borrower a general indication of what the money is costing him, not a precise mathematical indication—say within a quarter or one half per cent, it is possible to devise a definition of cost of money that will satisfy that requirement. It is technically a relatively complex matter.

The CHAIRMAN: Professor Neufeld, what do you think of this definition. This is the definition found in the Small Loans Act, section 2(a):—

... “cost” of a loan means the whole of the cost of the loan to the borrower whether the same is called interest or is claimed as discount, deduction from an advance, commission, brokerage, chattel mortgage and recording



fees, fines, penalties or charges for inquiries, defaults or renewals or otherwise, and whether paid to or charged by the lender...

and it goes on in terms more specifically linked to small loans. I thought it might be interesting for the committee to hear another attempt, which apparently has worked reasonably well over a period of years. Perhaps also our next witness, Dr. Ziegel, might give us his view on this because, I think, he has done some work in this area. Perhaps you may have some comment on this legislative attempt we already have.

Mr. NEUFELD: That definition in the Small Loans Act is completely consistent with my view of what constitutes interest rate. It is the cost of money.

The CHAIRMAN: And you feel that a similar definition could be drawn up to cover the cost of borrowing from a bank.

Mr. NEUFELD: Yes, I do.

The CHAIRMAN: The commercial side of loaning, and so on.

Mr. NEUFELD: Yes.

Mr. FLEMMING: Professor Neufeld, you say that the various small charges that the chairman has read out of a statute in connection with the Small Loans Act is the total cost of money. If a person has an account in the bank and within fifteen or twenty days he issues cheques to the amount in the account then you could say that actually his bank is doing his bookkeeping. In such a case do you consider it appropriate that a charge be made for this service.

Mr. NEUFELD: It would be completely appropriate because they would be imposing such a charge on people who might not have a loan. The charge would not be based on the loan made; it would apply to people who did not have loans and people who had loans. It would be a separate thing.

The CHAIRMAN: Dr. Neufeld, would not a more appropriate term than "the cost of money" in the context in which we are using it, be "the cost of borrowing" or "the cost to the borrower?"

Mr. NEUFELD: Well, you borrow money, and I would not want to argue with that.

The CHAIRMAN: The reason I mention that is that otherwise it would be easy for people to try to limit the definition to the loan account side of the balance sheet, in trying to draw a distinction.

Mr. NEUFELD: I think the cost of borrowing money is perhaps the best way of looking at it.

The CHAIRMAN: This is what you are driving at?

Mr. NEUFELD: Yes.

(Translation)

The CHAIRMAN: Mr. Latulippe.

Mr. LATULIPPE: Mr. Chairman, I would like to ask the witness why we have this increase in the interest rate? Is it because the banks feel that they must increase their income by increasing the interest rate, their profits being inadequate?

(English)

Mr. NEUFELD: I think that increasing the interest ceiling would not necessarily mean that the profits of the banks in terms of the rate of return on the capital of the banks would be increased, simply because by increasing the rate of interest on loans, it should be possible for the banks also to increase the rates that they pay to savers on deposits—and that would be an increased cost. I would not assume that it is obviously the case that the bank's profits or rate of return on capital would rise because of the freeing of the rate. Certainly I would not argue that one should free the rate because one should improve the profit position of the banking system. I would argue that one should free the rate because one should get a better allocation of the capital of the country.

(Translation)

Mr. LATULIPPE: Mr. Chairman, if we increase the interest rates, this will necessarily increase the cost of living, just as every other element in the economy increases the cost of living. We are in a period of inflation and there is no stop to this increase in the cost of living. This manipulation in the interest rates is going to raise the cost of living and there is no solution to this problem. How would you solve it? Is there a solution to the rising cost of living in the raising of the interest rates for the banks? Will this improve the economy?

(English)

Mr. NEUFELD: I do not think it will increase the cost of living because I would expect that as a result of the changes in the bank act that the cost of borrowing money to some people will fall while the cost to others will rise. I would not expect that the average cost of money in the country as a whole would rise as a result of the removal of the interest rate restrictions.

In other words, people who now have to go to non-bank lenders to obtain money at various high rates of interest, might well have access to the banks at a lower rate of interest.

(Translation)

The CHAIRMAN: Have you completed your questions, Mr. Latulippe?

Mr. LATULIPPE: The interest rate of the Bank of Canada has stepped up from  $1\frac{1}{2}$  per cent in 1934 to  $6\frac{1}{4}$  per cent and, in a famous conversion of government bonds, \$6,600,000,000 were renewed at 4 and 5 per cent instead of  $2\frac{1}{2}$  to 3 per cent. This is since the war. Is the present increase in interest rates going to have an effect on government bonds? Is it not going to lead to the same consequences?

(English)

Mr. NEUFELD: I do not think that the changes in the clauses relating to interest rate in the bank act will have the slightest effect on the price of government bonds. I think it would have no effect at all. There has been a general trend toward very high rates of interest, not only in this country but in all western world countries. This is a general indication of the shortage of capital in economies that are fully employed. This change merely relates to one of a great many interest rates in the economy. Those interest rates in general are what they are, not because of legislative restrictions but because of a very strong demand for capital.

(Translation)

Mr. LATULIPPE: I have received letters from citizens from the riding I represent, people who have bonds and have had them for some years, and due to the increase in interest rates, they want to sell their bonds. I get letters asking me to intervene with the government to help them in transferring these bonds to present issues. This indicates that the interest rates are going to increase. People are going to pay for this. I do not see how you can justify the statement that increasing the interest rates is not going to increase the cost of living. I do not understand your stand at all. Have you no other explanation to give me?

(English)

Mr. NEUFELD: The explanation that I have is essentially this. In my view, the interest restriction in the Bank Act had no effect whatsoever on the cost of money in general in the country.

Secondly, the interest rate restriction in the Bank Act has had the effect of denying bank credit to people who have to borrow elsewhere at very high cost. Therefore, the removal of those restrictions will lower the cost of money to some people just as it will raise it to others, and it is questionable whether on balance it will raise the cost of money to the people who are prospective and existing bank borrowers.

Again I would say that I do not think that high interest rates lie behind the increase in the cost of living. Indeed I would say that the movement towards high interest rates, which should encourage saving, would have the opposite effect; it would work against an increase in the cost of living rather than add to it.

(Translation)

Mr. LATULIPPE: Today, sir, we find that governments, provinces and municipalities, companies, school boards, public buildings, corporations, religious organizations all are issuing bonds at interest rates of  $7\frac{1}{2}$  and 8 per cent. Why is there this shortage of money? Why these prohibitive rates on capital which generally speaking has been spontaneously generated?

(English)

Mr. NEUFELD: I think that the main reason is everybody wants to borrow money, that there has been a tendency for the country to try to do too much too quickly and that this very strong demand for borrowed money has driven up the price of money. I think that is the principal explanation for it.

I might say, that I personally do not feel very sorry for borrowers because while it may appear that they are paying a great deal for money, the fact is that most of them are going to pay that money back in depreciated dollars because of the rising price level over the years. The people who have been hurt in this process have not been the borrowers but the savers who have seen the real value of their bonds decline because of the increase in the cost of living year after year.

(Translation)

Mr. LATULIPPE: Mr. Chairman, at the time of the revision of the Bank Act in 1954, the bank rate was raised to 6 per cent, and at the same time the bank



shares interest rate of  $8\frac{1}{2}$  per cent was removed and now they bring in 20 or 30 per cent. The Royal Bank, seventy-five cents every three months, that is an increase of \$3.00 a year for a share of \$10. The Bank of Montreal: four times \$0.55 is \$2.20, or  $17\frac{1}{2}$  cents special dividend, a total of  $\$2.37\frac{1}{2}$  per \$10 share. Now if we find that the banks—that the banks have reasonable income, whereas no restrictions are put on the increase in interest rates, who is going to put a stop to this increase in rates of all sorts, which certainly do contribute to increasing the cost of living and make it increasingly difficult for large numbers of citizens to pay their bills?

(English)

Mr. NEUFELD: The only comment I would make is that it is very difficult to argue on the basis of financial information that the rate of profits in the banking system is out of line with the rate of profits in other businesses and institutions. While I am very sorry that I could not follow through the arithmetic of the numbers you quoted, I have not had the impression that the rate of return on bank capital has been out of line with that earned elsewhere.

(Translation)

The CHAIRMAN: Any other questions?

Mr. LATULIPPE: I'll come back

(English)

Mr. GILBERT: I had a question, Mr. Chairman, but you asked it.

The CHAIRMAN: I accept that as a compliment. Are there any further questions on the area of rates of interest?

(Translation)

Mr. CLERMONT: Mr. Chairman, Mr. Latulippe is mentioning \$10 shares. Does he mean the cost of shares on the present market? Bank shares are not at \$10. Oh, no. Oh, no, they are not.

Mr. LATULIPPE: Bank shares are all at \$10.

Mr. CLERMONT: Oh, no. Not on the market. Not on the market. Oh, no. they are not. Not at all. On the market, the bank shares are not \$10.

Mr. LATULIPPE: Perhaps you could tell me, Mr. Ziegel. The banks have not the right to increase shares above \$10.

The CHAIRMAN: That was the cost at issue, but the cost on the market is different. This is the question in your mind, is it not, Mr. Clermont?

Mr. LATULIPPE: The market price is different, but that is a detail.

The CHAIRMAN: We might possibly return to this detail later. If there are no more questions on the topic of interest rates, I would suggest that we go over to debenture borrowing.

(English)

In English we say debenture borrowing. Do we have any further questions on this topic?

Mr. CLERMONT: Can I ask a general question, Mr. Chairman?

The CHAIRMAN: Oh yes. We are moving along so we can get to the general questioning. If I may put it this way, we are, on the home stretch with regard to the topics that Dr. Neufeld has raised. We have touched on debenture borrowing in the general context of bank operations and interest rates. Are there any direct questions on this topic?

Mr. MORE (*Regina City*): I have just one question.

The CHAIRMAN: Yes, Mr. More.

Mr. MORE (*Regina City*): The professor recommends a change from 10 per cent to 15 per cent in this field. In line with your reasoning of the effect on competing institutions you do not think this is too great a change at this time?

Mr. NEUFELD: No, I do not. I actually computed what it would probably amount to and it seemed to me that in view of the size of the competing institutions this would not cause any problems, particularly if there was provision for these other institutions to apply for bank charters.

The CHAIRMAN: I would suggest to the committee that we now pose any questions we have to Professor Neufeld on the topics of cash reserve ratio and secondary reserve ratios.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): On page 9 of your brief, Professor Neufeld, you say:

...the new legislation should require each bank to indicate annually to the Bank of Canada what it wishes its minimum cash ratio to be for one year ahead. This would enable the Bank of Canada to compute a fixed minimum cash ratio for the banking system as a whole which is useful for purposes of monetary control...

Are we to understand from that that you feel the consensus of banks on the desirable cash ratio would be the deciding factor on what the cash ratio provisions would be across the system?

Mr. NEUFELD: Yes, because the only thing that is important for purposes of monetary control is that there is some fixed cash ratio. Some argue that you need not have any cash ratio but I would not be prepared to go that far at this stage. However, one does require a fixed cash ratio for purposes of monetary control. It does not much matter whether it is fixed at 5, 6, 7, 8 or 9 per cent as long as you know what it is. The other point I would make is that any fixed cash ratio as such is not very useful from a commercial banking point of view because those are reserves that the banks by and large cannot use anyhow. On the other hand, it is true that there are differences between banks. Some banks have more savings deposits; some have less, and some have more long-term loans and some have fewer long-term loans. Some are heavier in the instalment credit business than others and so it goes. So there are differences between banks. It is because of these differences that it is reasonable to argue whatever the minimum cash ratio is, it should not necessarily be the same for every bank. It should be understood that the bank bill accepts this view by imposing 12 per cent on savings and 4 per cent on demand. The over-all cash ratio that the individual banks will adhere to will differ one from another. So the principle that there should not be the same minimum cash ratio for every bank is accepted in the bank bill. I am going only one stage further and arguing that since it is accepted that there are

differences between banks one should include the possibility that those differences will arise not merely on the liability side of the banks' operations but also on the assets side and that the best group of people who are in a position to judge what the minimum target cash ratio should be are the bankers themselves. They are the ones that know the character of their assets; they know the character of their liabilities, and therefore they should be able to say what in their view constitutes a reasonable cash ratio for their operations. So for each bank to indicate what its cash ratio should be would be sufficient to give the Bank of Canada a fixed ratio which it needs for monetary control. Furthermore, it would permit differences between banks with respect to the cash ratio. I do think it would work very well indeed. I would make only point, which I actually made in my summary but did not include in my original brief. I think it should be clearly shown that this cash ratio that they designate is not merely a minimum cash ratio but a cash ratio which they accept as a target cash ratio because there will be the problem where a bank might say: "We declare a two per cent cash ratio", and then go on, in fact, to operate at 5, 6 or 7 per cent. I think that would defeat the purpose of it. So as long as the banks regard the cash ratio that they declare as a target cash ratio there would be no problem and it could be defined in these terms.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I gather that you do not agree with Mr. Rasminsky who told me in this committee, in answer to a question, that it was essential for his control of the monetary system to have the cash ratio of the chartered banks set at a higher level than the banks themselves would wish, because of the terms and words he used.

Mr. NEUFELD: I have not discussed this with Mr. Rasminsky or with any of the people in the Bank of Canada. I would simply say that I think he would mean by that that you should have a cash ratio which is one that they adhere to, and the one way of doing this is to set it higher than they themselves would want it to be because for purposes of maximizing profits they would always adhere to the minimum cash ratio.

I would say it is not necessary to set it higher than that as long as it is clearly understood by the banks that the ratio they declare is one they accept as a target ratio.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Thank you.

The CHAIRMAN: Are there any other questions on this?

Mr. MONTEITH: I know this will seem like an awfully naive question but I intend to follow it up. What exactly is the purpose of a cash reserve on demand notes or savings deposits?

Mr. NEUFELD: The major purpose of a minimum statutory cash ratio is that it permits the Bank of Canada to forecast more accurately the effect of its actions on the nation's money supply. If the bank can depend on the fact that the banks maintain an 8 per cent cash ratio then it can fairly easily predict what effect its actions will have on the size of the nation's money supply. If the banks do not adhere to a minimum cash ratio the bank can never be certain what effect it will have on the nation's money supply. I would see that as the major advantage of a fixed minimum cash ratio. As I mentioned before, I cannot see how a fixed minimum cash ratio is at all useful to a bank from a commercial banking point of view. It is, after all, cash that, in effect, they cannot use.



Mr. MONTEITH: Have you any comment on the possibility of their being paid interest on these deposits?

Mr. NEUFELD: I really think that one could argue that both ways. The banks, again because of their relations with the Bank of Canada, do have certain advantages. They have access to the banks; they can call themselves banks, and this is something that is not available to other financial intermediaries.

Mr. MONTEITH: Have they a case for it if they have to join a deposit insurance scheme?

Mr. NEUFELD: It may well be that they have a case for receiving a rate of interest on the cash balance.

Mr. MONTEITH: When the cash reserve first came into being was there not some element of safety reserve in mind?

Mr. NEUFELD: I do not think so. The minimum cash reserve ratio was introduced in 1934, if I remember correctly. It has been discussed by legislators as early as confederation but it was never introduced until 1934. Then it was set at 5 per cent. In fact, the banks, were maintaining throughout that period about 9, 10 or 11 per cent. So when the minimum cash ratio was first introduced it was a curious one in the sense that it seemed not to be relevant either for commercial banking or for central banking. It was really only in 1954 when the cash ratio was brought up to 8 per cent and the banks were induced—I think the word “induced” is correct—to move their ratio from the 10 per cent down to the 8 per cent, that the cash ratio really became an effective technique for purposes of monetary control.

Mr. MONTEITH: Then they were requested to add another 7 per cent voluntarily. At one stage this was also the purpose.

Mr. NEUFELD: There is a section in here on the secondary reserve ratio. I do not know, Mr. Chairman, whether you wish me to go into the secondary reserve ratio.

The CHAIRMAN: I think the committee had agreed with my suggestion that we deal with both of these topics together.

Mr. NEUFELD: Of course. The secondary reserve ratio was not introduced by legislation; it was introduced by informal agreement between the chartered banks and the Governor of the Bank of Canada. It was introduced at a time when the banks were reducing their liquid assets very rapidly for purposes of making loans. It was my impression that the bank was concerned at the volatility of the volume of the banks' liquid assets and that the imposition of the secondary reserve ratio would have the effect of diminishing the volatility of their very liquid assets.

Mr. MONTEITH: Are you in favour of maintaining this secondary reserve?

Mr. NEUFELD: No, I am not. I think that it should be removed and that there should be no provisions in the Bank Act for re-introducing it.

Mr. MONTEITH: Thank you.

The CHAIRMAN: Are there any further questions on this topic at this time?

(Translation)

Mr. CLERMONT: In regard to the secondary reserves, which is 7 per cent, it is suggested in Bill C-222 that it might vary from 6 to 12 per cent. Are secondary reserves not asked for by the Bank of Canada, on occasion, to control the money supply and credit?

(English)

Mr. NEUFELD: Yes, it is asked for by the Bank of Canada. I do not agree with the Bank of Canada. I do not think the secondary reserve ratio is necessary for effective monetary control. I think it introduces an unnecessary rigidity into the operations of the chartered banks. I would go so far as to say that its usefulness for monetary control is so marginal and so limited that even in that area, in my view, it will not make a useful contribution in future. For example, for the last several years, if one examines the banking statistics, the stable liquid ratio has been the ratio that would include cash, treasury bills, day to day loans and government of Canada securities to total deposits. That ratio has been at about 30 per cent and it has been remarkably stable at that level. It is not being controlled by legislation. This is a reaction of the banks to what they regard as desirable minimum liquidity standard. To my mind, there is no legislation, necessary to achieve a minimum liquidity position. The second point I would make is that the intention that this secondary reserve ratio will slow down the rate at which the banks move from liquid assets into loans in a period of expansion is virtually nullified by the fact that when they now move into a recession and build up their liquid assets it has, by definition, to be above the minimum requirement because this minimum liquidity position applies both to periods of recession and inflation. Now in a period of recession they will be dealing with a 15 per cent liquidity requirement to get more money because we are following an easy monetary policy; they build up their liquid assets over the top of this minimum requirement and then in the subsequent period they will be able to reduce it. You might say yes, but the provision includes the possibility that the Bank of Canada will continuously increase this ratio if they tend to do this. My view is that whatever marginal advantage is to be gained by this would be offset by the fact that it would impose increasing rigidity on the operations of the chartered banks.

(Translation)

Mr. CLERMONT: If the Bank of Canada did not have that right, if it could control the credit and money supply at certain periods?

(English)

Mr. NEUFELD: It is my opinion that if they did not have the technique of the secondary reserve ratio it would not materially diminish its ability to control credit and the supply of money.

The CHAIRMAN: I would like to suggest to the committee that since it is about 25 minutes to 6 and we have our other witnesses, Dr. Fiegel, with us—and we certainly want to make sure that we have an adequate opportunity to hear the views that he has put forth in his brief—unless there are some very pressing questions on this issue of reserves, we might consider moving on to the issue of foreign bank agencies at this time.

Mr. GILBERT: Mr. Chairman, may I ask a question at this time?

The CHAIRMAN: Yes. It was just a suggestion on my part.

Mr. GILBERT: Dr. Neufeld, you are aware of the proposed change in the legislation to change the monthly averaging of cash ratios to a bimonthly averaging. I would assume the reason may be the submission to the Porter commission of the Bank of Canada, where they indicated that the existing formula permits unduly slow responses and results in unduly large discontinuities in reserve requirements. What are your views on that?

Mr. NEUFELD: This is a question that is best answered by the technical experts, the cash managers in the chartered banks and the cash manager in the Bank of Canada. I have had an interest in the matter but I warn you this is the interest of an outsider rather than the interest of a professional insider. My views, in the absence of additional information, would be that the Bank of Canada's position is a weak one. I do not think that the fortnightly averaging is really all that necessary. I agree it might well marginally improve the ability of the Bank of Canada to predict short-term effects of its actions but when one considers that it would also impose substantially new burdens on the chartered banks in terms of reporting and so on, I am not at this stage convinced that whatever marginal advantage it would give the Bank of Canada would be justified.

*(Translation)*

Mr. LATULIPPE: I would have a supplementary question, Mr. Chairman.

The CHAIRMAN: Yes, Mr. Latulippe.

Mr. LATULIPPE: Could the witness please give us, for the Committee and the people, some idea about the inner bank reserves, the hidden reserves? What is the sum of these reserves, do you think?

*(English)*

Mr. NEUFELD: I am not a banker and they do not tell me very many things. I just do not know.

*(Translation)*

The CHAIRMAN: By definition they are secret.

*(English)*

I think we have had a general look at Dr. Neufeld's views on reserves. Perhaps we might see what questions the committee has about the views he has put forth with respect to foreign bank agencies and related matters.

Mr. NEUFELD: Mr. Chairman, may I make one remark about that section because there is one amendment I must make. I imply in the first sentence of that brief that the government has announced it will permit foreign bank agencies to operate. This is not correct. The government has not announced that it will permit foreign agencies to be established. I would simply strike out that sentence.

The CHAIRMAN: It has in fact said that it is considering the question, and it specifically invited this committee to look at it very thoroughly because it is very interested in our views on this topic. I presume it is equally interested in our



views on all other topics dealing with the legislation referred to us. I will recognize Mr. Cameron, followed by Mr. Clermont and others in the order in which they signify to me.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Dr. Neufeld, do you feel that the American banks would be particularly interested in establishing agencies in Canada? Would there be the scope for them here that the agencies of Canadian banks have in New York?

Mr. NEUFELD: This would depend entirely on the specific powers that would be given to the agencies. If foreign agencies in Canada were not permitted to solicit deposits from residents of Canada then I think the scope of the operations here would be very limited.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Is that not the case with the agencies in New York?

Mr. NEUFELD: That is true but because the financial centre is so much bigger there is an awful lot of non-resident money in New York which makes the operation profitable. On the other hand, I am not quite sure whether a Canadian bank operating in New York under New York state law cannot solicit deposits from a resident of another state.

The CHAIRMAN: I think that is the case.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Apparently they can do so. But is not the basis of their operations in New York their ability to pay more for American funds than is permitted to an American bank? The United States deposits are then transmitted and deposited with the Canadian bank in Canada. Is that correct?

Mr. NEUFELD: This certainly has been an important factor. On the other hand, the banks have been operating in New York for an awful long time—some of them over a hundred years, and I think that there are now a number of reasons for doing some banking business in New York. The fact that they have greater freedom with respect to interest rates is one reason the volume of that business is quite significant.

The CHAIRMAN: You talk about banks but you actually mean agencies?

Mr. NEUFELD: Agencies, yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The witness we had said although they could take deposits from other states, not residents of New York, they had not in fact done so to any great extent. So I imagine it is this other operation that is the important one. Do you think that there is a possibility, if they did establish agencies here, it might have some dislocating effect on the flow of capital back and forth across the border, in other words, that it would promote the outflow of Canadian funds to the United States?

Mr. NEUFELD: I do not think really the problem would be the one of encouraging a sort of secular long-term outflow of funds from Canada because there are no obstacles now to the outflow of funds. Because the channels, in fact, are numerous, funds flow very easily.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You mean there would be institutional channels established?

Mr. NEUFELD: Yes, but even at present there are almost no obstacles for funds to flow out if such funds want to flow out. I think that the issue is really one as to whether it would increase the volatility with which funds flow in and out. My own feeling is that it is impossible to predict in advance what would happen. So much depends on the way in which such agencies decide to operate and the kinds of powers they are given in Canada, and it was because of my frank admission that I just did not know the effect this would have on the flow of funds that I thought that it would be desirable to introduce agencies on a sort of trial period basis.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Of course that might not meet the demand for reciprocity that seems to be coming up now in connection with the vexed question we have of the foreign owned bank in Canada.

Mr. NEUFELD: Yes, although technically speaking—and I stand to be corrected on this; I am not speaking with great certainty—I think that the licences the Canadian banks have in New York are not indefinite licences. I think they have to be renewed yearly.

The CHAIRMAN: The agency licences are renewable and I presume terminable yearly.

Mr. NEUFELD: Yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I have heard it said that one of the reasons for the transaction that has caused so much furore, the acquisition of the Canadian bank by an American bank, was to some extent at least for the purpose of being able to establish an agency of an ostensibly Canadian bank in New York that could then do the sort of things that agencies of Canadian banks are doing now, and enable an American bank to get into the field from which it is now excluded. Would you think there would be any possibility that might be the case?

Mr. NEUFELD: I was a little bit confused by your question. I think at one stage you said Canadian banks in New York when you did not mean that.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): One of the reasons for an American bank having purchased a Canadian bank was to establish an agency in New York of this ostensibly Canadian bank, thus enabling the parent bank to get into that field?

Mr. NEUFELD: I will not answer your question because I just have no knowledge of that particular event.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Do you think it is conceivable that one of the reasons might be that it would be advantageous for it?

Mr. NEUFELD: I just do not know.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Thank you.

(Translation)

Mr. CLERMONT: This is one of my questions that was answered when the Professor suggested a correction to Bill C-222 concerning foreign bank agencies in Canada. I would quote your comment on page 2, and I quote:

(English)

At the same time the reduced competition arising from the restrictions on foreign ownership of banks in Canada will at least to some extent be compensated . . .

(Translation)

—would you have any objection to the Canadian Parliament granting charters to enable foreign banks to hold majority stock in a Canadian bank?

(English)

Mr. NEUFELD: If you will permit, I want to make two major points. The first that the principle economic advantage of permitting United States banks to operate in Canada, whether through the ownership of existing Canadian banks or through the introduction of new banks, is that this would increase competition in the Canadian banking system and would therefore probably lead to an economically more efficient banking system. The only economic disadvantage that I can conceive of, as a result of permitting foreign ownership of Canadian banks, would be that it might result in destabilizing capital movements into and out of the country. I think the weight of the argument on an economic plane would be that the introduction of United States banks into Canada would increase the economic efficiency of the Canadian banking system. So it seems to me that the issue is really part and parcel of the whole matter of foreign ownership of Canadian industry. I would think it is really a matter of whether the Canadian nation is prepared to suffer some economic disadvantages in order to retain ownership of its industry and financial institutions. On that plane I think my opinion is no better and no worse than the ordinary man in the street because, as I say, it is essentially a political issue, and on such political issues I think my own view is no better than anyone else's because I would not be speaking as an economist.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Could I ask a supplementary? You spoke of increasing the efficiency of the Canadian banking system. Could you be a bit more explicit about how it would affect the efficiency of Canadian banking.

Mr. NEUFELD: I think that some of the large American banks have become exceedingly efficient in terms of the way they go about their business, the kinds of people they have running their departments, the development of specialized departments within banks and all the rest of it. It is my impression, merely as an outside observer and nothing more, that Canadian banks would benefit from the kind of competition that would come from one or more of the American banks that are in the forefront of the development of efficient banking.

Mr. MORE (*Regina City*): Do you think that our banks are stuffy institutions then?

Mr. NEUFELD: I would rather say that I think there is still room for improvement.

The CHAIRMAN: You are being very diplomatic.

(Translation)

Mr. CLERMONT: Probably you are aware of certain American laws that do not permit foreigners to conduct banking operations in certain States. In other



States, there are very liberal laws. I think about forty states will not allow foreign banks in. Is there a foreign bank in the United States that is authorized to work on a national level? I am not speaking of the Canadian banks, but of banks that are foreign, whether it be French or British banks or banks from some other country. Can they work on a national basis in the United States?

(English)

Mr. NEUFELD: It is my impression that they could not do so. I would ask you to accept this as a very unauthoritative answer.

Mr. CLERMONT: Thank you.

(Translation)

Mr. LATULIPPE: What would be in the interest of Canada? Would it be to encourage the establishment of foreign banks in Canada, subject to the same conditions and regulations as is the case of branches of banks we have now? Would there be advantages for Canada in having other banks alongside the ones we now have, although making these foreign banks subject to the rules and regulations applicable to Canadian banks?

(English)

Mr. NEUFELD: Strictly from an economic point of view I think the argument, on balance, is that it would be desirable. However, ignoring all the economic logic of the argument and just speaking from a point of view of sentiment and emotion I, personally, would not want to see ownership of the Canadian banking system move into foreign hands.

The CHAIRMAN: Professor Neufeld, is not sentiment and emotion the basis on which countries, to a large extent, come into being and stay in existence?

Mr. NEUFELD: I do not know; it may be.

Mr. MORE (Regina City): You were not around in 1866?

Mr. NEUFELD: No, I was not.

The CHAIRMAN: We will accept that answer. Speaking as an individual, not as a professor of economics, would you agree with the assertion that sentiment and emotion are important factors if not with regard to the coming into existence of a nation or country, certainly with regard to the continuing existence of a nation or country?

Mr. NEUFELD: They are certainly an important factor in my own life and I would think they are in the life of a nation.

The CHAIRMAN: Do you have further questions on this topic at this time? I suggest to the committee that Dr. Neufeld has made his argument rather clearly with respect to the issue of prohibition of loans against bank stock and unless there is some specific questions on that point perhaps we could address general questions, if there are any, to our witness in the remaining five minutes before six o'clock.

(Translation)

Mr. LATULIPPE: A general question, Mr. Chairman.

The CHAIRMAN: Mr. Clermont indicated that he wishes to put a general question, that is why I mentioned that. But I cannot allow you to do the same thing.

Mr. LATULIPPE: You have allowed Mr. Clermont to get ahead of me.

The CHAIRMAN: No, Mr. Clermont has changed his view.

Mr. LATULIPPE: I had put a question, when I was beginning my question period. Why are the holdings of the Caisses Populaires or the near-banks not included in the money reserves, nor those of the trust companies? Why do they not form part of the money supply? Why do their holdings not come into the money supply?

(English)

Mr. NEUFELD: They do come into it. I think an economist would argue that they are part of the nation's money supply.

(Translation)

Mr. LATULIPPE: I have another question I put two weeks ago. I think it was Mr. Gibson I put it to. He told me that these institutions' holdings do not form part of the money supply.

(English)

Mr. NEUFELD: If that is a correct interpretation of Mr. Gibson's remarks I would have to disagree with him.

The CHAIRMAN: It is six o'clock. We have another very distinguished witness who has come down from Montreal this afternoon to be with us and I think we should give him the opportunity of putting forward his views after we have recessed for supper.

On behalf of the committee, Dr. Neufeld, I would like to thank you for your very useful presentation and discussion. We will recess until eight o'clock this evening.

#### EVENING SITTING

The CHAIRMAN: Gentlemen, I think we should resume our meeting. Our witness this evening is Dr. Jacob Ziegel, Professor of Law at McGill University. He took degrees in law, a bachelor's degree, master and doctorate at the University College, London. He came to British Columbia after having first been admitted to the British Bar. He was admitted to the British Columbia Bar and practised there for several years. He then became professor of law at the University of Saskatchewan Law School and, then, as I have indicated, he came to McGill Law School. He has specialized in the field of commercial law, consumers' rights, creditors' rights, personal property and so on.

I think I should indicate to the Committee that when I asked the Clerk to contact the Consumers Association informally and unofficially to note their intentions with regard to a brief they said they knew that Professor Ziegel was submitting a brief and that since much of what they wanted to say was incorporated in his brief they were, in fact, not intending to submit one of their own. I think this is a high recommendation for our witness this evening. I have

explained to Professor Ziegel our procedure and I therefore invite him to present his brief to us at this time.

Professor JACOB S. ZIEGEL (*Professor of Law, McGill University*): Thank you very much, Mr. Chairman. I would like to say what a privilege it is for me to be able to appear before the Committee tonight and to offer such views as I have on the new banking bill which is before the Committee. Mr. Chairman, however, I feel it is in order, before starting my formal presentation, to make what lawyers call a "plea of confession and avoidance." I am a shareholder in one of the chartered banks. However, I hasten to assure the members of the Committee that this fact has in no way influenced my views. In fact, it will be seen, as I develop my brief, that some of my views are quite adverse to what a good banking man should hold.

Mr. Chairman, my brief falls into five parts and since I understand the members of the Committee all have a copy of it I will merely summarize its principal contents. But, at the same time I would like to enlarge on some of the points that are mentioned in my brief and, if I may, also refer to several other points that have been raised at earlier sessions of the Committee that are not already referred to in my brief.

The first part of my brief, Mr. Chairman, deals with the elimination of interest ceilings, and I have tried to explain here why I support the recommendation of the Porter Commission that ceilings should be eliminated in toto. So when I refer to my support of the bill on this point I am not, Mr. Chairman, referring to the interim measures the government purports to introduce in Section 91. I am thinking in terms of the medium or long-range goal of implementing the recommendations in the Porter Commission. I give three reasons for supporting the bill on this point.

First is a legal reason but one which is very important all the same. That is, contrary to general assumption, the banking bill does not effectively limit the banks to an interest ceiling of 6 per cent. This somewhat startling result follows from the fact that this and all other banking acts have never attempted to define the term "interest." The Canadian courts, on the comparatively few occasions in which they have had to consider the term, have given it a very narrow meaning, with the result that by a certain interchangeable use of terminology the banks have been able to obtain a higher rate of return on a loan than the 6 per cent permitted in Section 91. A classical example of this technique is, of course, with reference to the consumer loans. I am sure the members of the Committee know as well as I do that the banks are obtaining an effective rate of return of between 11 and 12 per cent per annum, not the 6 per cent that Section 91 ostensibly purports to limit them to. I am not criticizing the banks for this factor, Mr. Chairman. All it shows, I think, is that Section 91 can be easily circumvented and in practice is. So even if there was no other, I think the practice with respect to consumer credit loans is a reason for altering Section 91.

My second objection to the present Section 91 is that by limiting the banks to a relatively low rate of legal return, it excludes precisely that class of borrowers who most badly need a source of low cost loans and are unable to find it outside the banking sphere. I am thinking in terms of small business and until fairly recently of consumers at large.

Mr. Chairman, the Porter Commission in its report drew attention to the fact that a very sizeable segment of the community was compelled to go to high



cost lenders in order to satisfy their financial requirements. Beyond the Porter Report we have several provincial reports, including a very detailed report published in Nova Scotia as a result of the royal commission inquiry presided over by Mr. Arthur Moreira. If I may, I would like to suggest the report is well worthy of study if one is in any doubt about what does happen outside the banking sphere with respect to those people who are compelled to look for loans. There was also a report in Ontario concerning so-called second mortgage lending. It again indicated the very high rates of interest that home owners were obliged to pay because they were not able—at least it was not believed they were able—to obtain loans from banks at the rate permitted in Section 91. So that is my second reason for supporting the long-term provisions in Clause 91 of the new bill.

My third reason is, that if one wanted to regulate the permissible rates of return on loans. Section 91 strikes me as being wholly arbitrary and the rational way of going about it. Loans like other types of commodities vary enormously from one to the other. The small loan is not the same as the large loan. One borrower is not the same as another borrower, so it should follow in the nature of things that the permissible rate of return on a loan should vary with the nature of the particular loan in question. But section 91 is wholly arbitrary. It does not permit banks to take into account the different factors that normally occur in the granting of any loan. If, by way of comparison, one looks at the Small Loans Act, one sees the Bank Act has taken into consideration at least one of the important elements in determining rate of return; that is, the size of the loan. Under the Small Loans Act there is one rate of return for loans up to \$300; there is a second rate for loans from \$300 to \$1,000 and there is a third rate for loans between \$1,000 to \$1,500. So these, then, Mr. Chairman, are my three principal reasons.

I have one reservation concerning the total elimination of interest ceiling and that is in the area of consumer loans. I deal with this question on page 4 of my brief. The difficulty, if it is one, arises in this way. The Small Loans Act regulate consumer loans up to \$1,500. It might be said that if banks are now free to charge consumer loans whatever they felt was an appropriate rate, this amounts to a discrimination. I do not myself believe that this would be a valid complaint but still it may have a certain measure of political potency. If the members of the Committee felt that it was a valid argument, then the question would arise: What ceiling should one place on the rate of return on consumer loans? I have suggested a ceiling of 12 per cent for a reason I give in my brief, namely, that all available statistics show that 12 per cent is adequate return for the average type of consumer loan made by the banks. I think the American statistics show this perhaps more fully than the Canadian. There is another reason which may commend itself to at least some of the members of the Committee, and that is that in most of the Canadian provinces, if not all, the Caisse Populaire—the credit unions—are restricted to a rate of return of 12 per cent so that by imposing a similar ceiling on bank loans you have what would at least appear to be a certain measure of consistency.

I would like, if I may, to comment on a proposal that appeared in Professor Neufeld's paper. He suggests, it will be recalled, that instead of lifting the ceiling on rates abruptly it should be done in stages by permitting a greater augmentation on the permissible rate of return. I can see one serious objection to that, Mr.

Chairman, and that is with respect to consumer loans. If we accept the fact that the banks are now in effect obtaining a rate of return between 11 and 12 per cent, what are you going to do with the banks under the type of suggestion put forward by Mr. Neufeld. It seems to me you are going to be impaled on the horns of a dilemma. You are going to say you are going to ignore what is happening in that sphere and continue as we have done hitherto. I think this is unsatisfactory. Sometimes we indulge in fiction because it is expedient to do so but there comes a point when it is neither eloquent nor political to ignore realities. I think we have reached this point with consumer credit. If you agree with me in this line of argument, then I think you would have to permit the banks to charge a realistic rate on consumer loans and this would immediately cut a very large hole into the gradual stat rate increase recommended by Professor Neufeld.

If, on the other hand, you say, no, all borrowers will be subjects to the same rate, then you are going to compel the banks, it seems to me, to abandon a large part of the consumer borrowing which they are carrying on so successfully at the present time. My personal feeling is that the banks should be encouraged to increase their loans to consumers and other small borrowers because it is, in effect, the lowest rate obtainable in any segment of the financial community.

The second part of my brief, Mr. Chairman, deals with the disclosure of the true cost of bank loans and here I am almost entirely *ad idem* with Professor Neufeld. I do, however, express some reservations not on the principle but about the desirability of extending the disclosure principle now to all forms of loans, and I stress that in principle I am entirely in agreement with Professor Neufeld, but as to the timing I have some reservations. My reasons for these are all the discussions which have taken place in the various legislatures—provincial and federal—with respect to this important question have essentially restricted themselves to disclosure in agreements to consumers. Several of the provincial acts dealing with this question, including those of Alberta, Manitoba and Ontario, restrict the disclosure principle to consumer loans. If you now decided that the proposed disclosure provisions in the banking bill should be extended to all forms of loans, this may create some difficulty in dovetailing the federal legislation with the provincial legislation. As I am sure, members of the Committee are aware, the provinces have shown great reluctance in promulgating new legislation because they said they first wanted to see what the federal government was going to do in its area of jurisdiction. If the federal government now intends to adopt a different yardstick or a wider yardstick of disclosure than the provinces have shown themselves interested to adopt, this may create new confusions, a new era of uncertainty and further delay in introducing what, I think, is generally regarded as very desirable and, indeed, very important legislation. My opinion is that a bird in the hand is better than two in the bush, and I would rather settle for disclosure legislation now, restricting it for the moment to loans to consumers, than try and attempt to cover the whole field of loans with the potential difficulties this may involve.

On the point of technical difficulties, perhaps, I may be permitted to add another point. The Chairman pointed out this afternoon, and I think I do, too, in my brief, that there is already a section in the Small Loans Act that gives a definition of the cost of a loan; it is an all-embracing definition. That kind of definition is, I think, easily applicable to a consumer loan not involving a mortgage on immovables or real estate. It is much more difficult to apply when you get into the sphere of real estate or very large transactions.



The reason is that when you are involved in immovables invariably the practice is for the lender at some stage of negotiation to want to have made an appraisal of the property and to incur other expenditures of a very substantial nature. I think it is a bit more difficult to tell a bank when you incur these expenditures and have made the debtor pay for them, they must be included in the calculation of the cost of the loan to the lender. I do not say it is impossible, but what I do say is that because of the much larger sums involved in a large transaction, you are dealing with a problem of somewhat different dimensions than where you are merely making a loan of \$1,000 or \$2,000 against the purchase of a car or some other household equipment where the bank is not involved in any substantial expenditures outside its normal overhead.

The third part of my brief, Mr. Chairman, deals with another area of disclosure requirement and looks as though it is slightly picayune, but I submit that it is not, that it ought to be considered seriously. I take as an example the kind of information or the lack of it that is now given to depositors in personal savings accounts. I point out that at the present time personal savings accounts are credited with interest every three months. However, they are only credited with the lowest amount standing in that account during the period in question. So that in practice you frequently have a situation where a man may have had a very substantial amount in his account for two months and 15 days and then because he withdrew part of that amount a few days shortly before the expiration of the three months accounting period, he found himself not receiving any interest at all. I do not criticize the result; what I do criticize is that there is nothing in the documents now handed to the saver in a personal savings account that explains to him how interest is calculated and on what basis. I feel that the depositor is entitled to have this information and that it should be prominently printed in the literature and in particular in the personal savings account book that is handed to the depositor at the time he opens his account.

I make the same observation with respect to the rates of interest the banks pay on a personal savings account. They seem to be remarkably secretive about it. I have made a point when walking into my own bank to see whether anywhere in the bank there was a conspicuous notice disclosing the prevailing rates of interest on personal savings accounts. I have not seen it and I have looked hard and banking associates have confirmed to me that they do not go out of their way to advertise the fact presumably because the rate is not that high, that attractive that they would want to unduly advertise it. Be that as it may, I think this is unfortunate; that in one way or another we should persuade our banks to be much more forthcoming in information relevant to their customers than they now are at the moment, and if necessary I would suggest the Bank Act be amended so as to require them to give some of the items of information I have suggested.

The fourth heading in my brief, Mr. Chairman, deals with the question of representation on the board of directors of banks. My complaint under this heading is that reference to the composition of the board of directors of any of our banks will show that they are almost exclusively made up of businessmen. Perhaps, I can quote some statistics, Mr. Chairman, without mentioning the banks by name.

At the end of 1965, one of our largest banks had 44 directors, four occupy executive positions in the bank; 34 are active businessmen of repute and consid-



erable responsibility in the various businesses with which they are connected; four are lawyers apparently in active practice and apparently also with close business links; one was a retired general who I assume is also now engaged in business—hopefully a lucrative business—and there is one who, so far as I could interpret his position is a member of a foreign government; perhaps he is a member of the legislature. The fact remains, Mr. Chairman, out of these 44 directors, a very large number, not a single one by any stretch of the imagination could be said to represent any of the important customers of the bank outside the business sphere.

Now, who are the important customers of the bank? Statistics, Mr. Chairman, are available in the schedules or the exhibits to the brief which the Inspector General filed with this Committee in its hearings. Further figures are also available in the Porter Report. They show that the banks do 52.4 per cent of their business with businesses in which I include every type of business, and the rest is done with other segments of our community. A very large share is done with ordinary individuals like you and me, to the extent of almost 30 per cent. A very substantial volume of business is done with municipalities and other government departments.

If one looks at the liabilities of banks one finds that the banks obtain almost 40 per cent of their deposits from individuals, mainly in the form of personal savings depositors, and if one added to the figure for personal savings depositors the number of individual current depositors, I think one would get a figure of close to 50 per cent. So I think all this shows that the banks' customers are by no means restricted to businesses of one kind or another; the rest of the community is awfully important to them. Therefore, I think it not unreasonable to expect the banks to have a broader representation than they have at the moment and I have urged, if it is necessary, that the minister be empowered to compel the banks to have a more broadly based representation than they do now.

In this connection, Mr. Chairman, it seems to me that the Bank Act should be amended so as to encourage a greater degree of democratization among the directorships of the banks and the conduct of the banks' corporate affairs.

If we look at the directorship requirements of the current bill, we find that clause 18(2)(c) requires every director of a bank by way of qualification to hold at least 500 paid up shares at a par value of \$10. This would amount to \$5,000 if the shares were, in fact, sold at par value. However, as one of the hon. members pointed out this afternoon, the market price of bank shares at the moment is well above the par value and so it may well be that a man who is interested in becoming a director of a bank today would need to invest more like \$35,000 or, perhaps, as much as \$40,000, even to be eligible to stand for nomination. I think this is an unsatisfactory position and I would suggest that the qualification figure should be substantially lowered. It may be said that a high degree of investment by a director is for the safety of depositors and shareholders; I disagree. We have had several major scandals in the financial community recently in which very prominent and large shareholders were involved. I do not believe that experience shows that probity and large shareholdings necessarily go hand in hand; quite the reverse may be the case. Conversely, we frequently find that people with very modest investments—indeed sometimes none at all—render a sterling service to the organizations with which they are connected. It is appropriate perhaps that I should mention cabinet ministers, or perhaps on a more modest

level I may mention the numerous officials across the country who are connected with credit unions and Caisse Populaire. No one suggested that before one can become a trustee or a director of the Caisse Populaire one should have a very large deposit on account.

The question is, what kind of shareholding qualifications should be necessary for directors? I would suggest either that it be drastically reduced to something like 10 or 20 shares, or, alternatively, that it be coupled with the prospective remuneration that the director may expect in his new office: for example, a shareholding equivalent to the directors' fees paid during the year of his election.

There is another recommendation I would like to make in this connection, and that is that the director has ten days within which to qualify himself in his new position. The existing statutory requirement is that he must have this qualification at the date on the day of his election, and quite apart from other considerations this can create hardship. The Canada Corporations Act of 1965 gives the director of federal companies a ten day period in which to qualify himself. I suggest a similar amendment should be introduced in clause 18 subsection (2)(c) of the present bill.

There is a further matter that gives me concern, Mr. Chairman, and that is the use of proxies in connection with the election of directors of our banks; and indeed with the regulation of corporate banking affairs generally. Let me emphasize at the outset that I am not singling out banks for attention because they are worse than any other corporation; they are merely following standard practice. What I am criticizing is standard practice among all our major corporations. The practice I am criticizing is that with the notices of meetings that are sent out the shareholders are invited to sign a proxy in which he confers blanket authority to management to vote as they see fit both in the election of new directors and with respect to other decisions that have to be taken at these meetings.

Now, this is not a new problem in Canadian company law; it is one that received extensive attention in recent report in Ontario by a committee known as the Attorney General's Committee on Security Legislation. With your permission, Mr. Chairman, I would like to read two extracts from the report of that committee, which was published in March 1965. I am quoting from page 49. The first extract I should like to read is as follows:

In these days of large public companies with numerous shareholders, who as a rule do not have a voice in management of the company, the proxy assumes major significance in the control of companies. In most cases, management of public companies sends out proxies in a form that invites shareholders who are unable to attend meetings in person to appoint only nominees of management to vote at meetings of shareholders. In this way, there is a marked tendency for management to perpetuate itself in office. Further, proxies have been solicited to approve corporate action in cases where the shareholders have not been given sufficient information on which they could reasonably be expected to come to an informed decision.



Then, further down the same page the committee quotes from a statement by Professor Louis Loss of the Harvard Law School, the author of the best known text on American securities law. This is what Professor Loss said:

Corporate practice has come a long way from the common law's non-recognition of the proxy device. The widespread distribution of corporate securities with the concomitant separation of ownership and management, puts the entire concept of the stockholders' meeting at the mercy of the proxy instrument. This makes the corporate proxy a tremendous force for good or evil in our economic scheme. Unregulated, it is an open invitation to self-perpetuation and irresponsibility of management. Properly circumscribed, it may well turn out to be the salvation of the modern corporate system.

Now, I submit, Mr. Chairman, that Professor Loss's comments are completely opposite with respect to the provisions or the lack of provisions in the Bank Act dealing with the internal regulation of the banks. The banks are not subject, Mr. Chairman, to the provisions of the Canada Corporations Act. So that even if the provisions of that act were satisfactory—and they are not—it would not help us with respect to our Bank Act. Since parliament has undertaken to tell the banks, in the Bank Act, how they should regulate their internal corporate affairs, why not try and see that those internal regulations reflect the best modern thinking on the subject. In my opinion, the present provisions are at least 50 years out of date, and the time is well over due when those clauses—like clause 18, and the cognate clauses—are thoroughly reviewed.

The banks are very important corporations in our economy, and I think it is important that their corporate affairs should set an example to the rest of the corporate community. They would set an example if parliament saw its way to amend the banking bill so as to cure such defects as the present proxy system, such as the lack of the requirement for dealings by insiders in the shares of the company and similar provisions.

Before concluding this aspect of my summary, Mr. Chairman, I might say that following the report of the Attorney General's Committee in Ontario, the Ontario legislature adopted a new securities act and important amendments to the Ontario Corporation's Act earlier this year. Those provisions have adopted in their entirety the recommendations of the committee concerning the use of proxies by companies. I respectfully suggest that serious consideration be given to adopting similar provisions in the bank bill.

Mr. Chairman, the fifth and last part of my submissions deal with the security provisions in the bill, a somewhat technical subject, but one of considerable importance. I begin by pointing out that I support the recommendations of the Porter Commission that banks should be free to take whatever kind of security for loans that seems appropriate to them. I do express some regret that having adopted this important recommendation in clause 75 subclause (1) (c) of the bill, the draftsmen did not then proceed from this premise and revise the other sections in the act dealing with the taking of securities by the banks. I do not think it would be too sweeping a generalization to say that those clauses, or at least a good many of those clauses, are badly in need of overhaul and revision because they have grown up haphazardly over the years; literally a period of almost 100 years. They are not rational either in concept or in execution. So that,



therefore, they are pragmatic. From the point of view of principle there is much justification for reviewing them in their entirety.

Let me look in particular at section 88 and see how the future conjunction of clause 75 (1) (c) and the existing clause 88 is going to create all kinds of difficulties. Clause 75 (1) (c) says that the banks are free to take any kind of security; but if we look at clause 88 we see that the banks may take certain types of securities from certain types of borrowers. This immediately creates the impression of a conflict between these two sections; they are not easily reconcilable.

At the very least what the draftsmen ought to have said was that without prejudice to Clause 75(1)(c) a bank may take foreign types of securities. But I think even this minor modification would not be sufficient, because you still have all the other anomalies with respect to Clause 88. I think the first question we must ask ourselves—the question that the hon. Mr. Fulton also raised in an earlier meeting of this Committee—is: do we still need Clause 88? Clause 88, I think, goes back to 1890, and was primarily designed to accomplish two things: on the one hand, it was adopted as an exception to the rule which then prevailed, that a bank may not take goods as security. Clause 88 was to be an exception to that rule, because the government wanted to encourage the extractive and agricultural industries in the country. Since then, all kinds of further exceptions have been added to Clause 88. Now, Clause 75 has removed the remaining restrictions; therefore, do we still need Clause 88?

The only reason that I can think of for retaining Clause 88—and it is not a negligible reason by any means—is that provincial legislation is not yet sufficiently modernized and streamlined to enable the banks to take a safe and sound security. It seems to me, however, that once the provinces have modernized the legislation so as to enable the banks, for example, to take inventory on a manufacturer's stock, or a wholesaler's stock, simply as they now can under Clause 88, then section 88 ought to be repealed.

Now, Mr. Chairman, there are important movements afoot at the moment in several of the provinces, including Ontario, Quebec, and some of the western provinces, to rationalize and modernize the technical rules concerning the giving of security in what is called personal property. I think, therefore, this is an ideal opportunity for the federal government to provide neuter leadership by attempting to seek agreement with the provinces on a common set of rules that could be applied equally to securities given by provincial lenders and federal lenders. What we have at the moment is at least three different sets of rules. You have one set of rules applied to a provincial lender; you have another set of rules applied to a federal lender such as a bank that is using Clause 88 securities; you have a third set of rules where a bank is lending security, not under Clause 88, but under one of the other sections of the Bank Act, that still have to comply with provincial requirements. It seems to me, Mr. Chairman, that the position could be considerably simplified.

Another observation I would make about Clause 88 as it is presently drafted is that it is still too restrictive. It does not, for example, permit a bank to take security on the inventory of a retailer. Frequently, however, his inventory, his stock in trade, is the only collateral that a small shopkeeper can offer the bank. I have been advised by responsible bank officials that this has inhibited them from time to time in granting loans to small retailers. I think at the very least Clause

88 should be amended so as to authorize the banks to take as security the inventory of retailers in the same way as they are now permitted to take as security the inventory of wholesalers and manufacturers.

I would like also, still in connection with Clause 88, to make a brief reference to a new subclause Mr. Chairman, in which I believe you have a strong interest. That concerns Clause 88, subclause (5)(b) dealing with the priority of a growers claim against a processor. My sympathies are very much with the grower, but I question whether the proposed amendment is the best way in which to resolve the conflicting, and, I submit, the perfectly reasonable claims of the two parties in question, namely the banks and the growers. I think the problem which may arise is that the bank that is now being asked to extend a loan to probably a small processor may be faced with the possibility that there may be future claims by growers and may be extremely reluctant to lend to the processor. The result would be that his funds would dry up, or at least be substantially reduced consequently he may have difficulty in maintaining a full scale operation. I am sure you would agree that this is not the result you would want to accomplish. On the other hand, we also want to try and provide protection for the grower. I think we can attain both ends this way.

We could require the grower to file, in an appropriate office, notice that he is selling goods on credit to the grower. This would enable a bank to determine, before extending a loan, whether or not they are likely to encounter conflicting claims from a grower. If, of course, there already was on file such a notice from the grower the bank would enter the picture with its eyes wide open. Now my suggestion is—do not think it is a novel one; it already finds a place in a prospective bill currently being considered by the Ontario government called the personal property security legislation bill. I have a copy with me Mr. Chairman and I would be very pleased to leave it with you. Clause 35 subclause (2) of that proposed bill deals with the kind of problem you are faced with in Clause (5)(b) that it provides, as I have suggested, the person who is forced to sell goods on credit and wants to have a lien on them for his price, may file the document and where necessary also notify the prior inventory financier, so that the inventory financier knows that a new man has entered the picture and can govern himself accordingly.

I would like to conclude, if I may Mr. Chairman, with a brief reference to Clause 75, subclause (3) of the bill. That clause deals with the taking of security in immovables and limits the banks to 75 per cent of the value of such security. I am aware Mr. Chairman, that this figure is based on similar percentages in our mortgage and loan companies bank, but I think it is open to a number of objections. First of all, it will create difficulty where a bank is taking as security both movables and immovables. Clause 75 subclause (3) has nothing to say on this problem. Will the bank have to apportion its loan, with so much allocated to the immovables and so much to the movables. I think this would be highly artificial. So I think that in any event the subclause should be amended to make specific reference to a security on mixed collateral.

Then, again, you may encounter difficulties where a bank proposes to make a loan in conjunction with another lender. This is common practice in the mortgage field; it has become much more so in the last year or two. The advantages of a joint loan or a combined loan is that it enables the lenders to lend a higher percentage that they would otherwise be willing to. I think from



the point of view of a home owner this is a desirable trend. To the extent that Clause 75 subclause (3) would inhibit the trend, it would be a step backwards. Again it seems to me that clause 75 subclause (3) will create anomalies. Take the case of a man who wants to buy a home. He does not have enough to meet the full down payment, he goes to his bank and asks for a loan. Now, if there is already a mortgage on the property to the full extent of 75 per cent, the bank of course will automatically have to turn him down, quite apart from the fact that it is a first mortgage. But the bank could say, "you are reputable, you have a good job, so we will lend you money without collateral of any kind; or we will take your automobile as security instead."

It seems to me illogical that if the bank can grant loans in any size, for any amount, without any sort of collateral, we are going to deny it the right to grant a loan on the collateral of mortgages simply because the loan will exceed 75 per cent of the value of the property.

It seems to me that clause 75 subclause (3) is discriminatory. The clause as presently drafted permits a bank to purchase mortgage bonds for any amount regardless of the value of the underlying security. Now, I appreciate there may be sound commercial reasons for this exception, but I submit that the soundness for the reason apply generally to the whole field of security on immovables.

Finally, Mr. Chairman, I think we are mistaken in analogizing the situation that confronts mortgage loan companies and the banks. They are really in different positions. Mortgage and loan companies put all their eggs in one basket. They are only permitted to lend against the security on immovables. The bank, on the other hand, has a wide range of collateral, so that the danger of putting all their eggs in one basket is much less than it is in the case of mortgage and loan companies.

I did have a number of other observations, Mr. Chairman, but I am afraid I have talked awfully long.

The CHAIRMAN: Not at all; you have extrapolated on your brief and I have some new ideas. I suggest to the Committee a slight departure from our usual procedure. It appears to me that Dr. Ziegel has put forward some points which have not been touched on at all by previous witnesses, or if they have been, in a very limited fashion. The new points seem to be those towards the end of his brief, and perhaps we could look at the points in his brief in reverse order. How does that suggestion strike you? Because, as I say—without derogating from the value of some of his comments on interest ceiling and so on, we have touched on them to some extent,—Dr. Ziegel has dealt with some areas which I do not think have been touched on at all as yet. I think that in the time available for discussion we perhaps should give priority to the items which we have not looked at until now. Perhaps I should recognize you, Mr. Lambert, not only because you asked me first, but, because of your experience as counsel, you might be able to engage in some useful exchanges with our witness, dealing firstly with the topic security provisions in Bill No. C-222.

Mr. LAMBERT: Well, Mr. Chairman, this may result in a sort of an exchange of opinions between lawyers, and I hope I will not fall into that trap. But, first of all, I was very much interested in what Professor Ziegel had to say with regard to the taking of joint security on both real and personal property. Well, coming from a province where one would not dare step into this sort of trap, because in



Alberta we have the Judicature Act which limits your security to the value of the real property and if you elect to go on that you have had it. Secondly, under the Alberta Seizures Act if you seize personal property you are limited to the value of the property you seize; there is no, shall we say, personal deficiency or residual deficiency, on which you can then sue the debtor. So that a bank stepping into this sort of trap I think would be very ill advised. Therefore, you elect; you are going to go on to either a mortgage on real property for a specific sum, or a mortgage on personal property for a specific sum. If you dare blend them you do so at your own peril. However, I do not know, in other Provinces, there may be some complications. I am rather more interested in Clause 88, and the observations that Professor Ziegel has made there.

I must say that I do not quite agree with him in that I think that Clause 88 is still a very useful tool, notwithstanding Clause 75, there are, because of these matters, as I said, the Alberta Seizures Act with regard to personal property, and the difficulty of the chattel mortgage where there is an absolute conveyance of right, title and interest in the property, which is not done under Clause 88, security; there is an assignment of interest on that. But, I would find it very difficult to be able to assign right, title, interest to goods in process as you would under Clause 88. To me, Clause 88 does provide a useful tool. True, there may not be quite the same requirement for certain types of production, but I cannot see the general conflict between Clause 88 and Clause 75 as was seen by Dr. Ziegel. To me they each have its own purpose.

However, I would like to put one point to Dr. Ziegel. Has he considered the upsetting of the priorities under Clause 88 (5) (b) with the Bankruptcy Act. Under the Bankruptcy Act the secured creditor, that is, the bank under Clause 88, has the priority. However, Clause 88 (5) (b) places claims for wages, upsets, as a matter of fact, the schedule of the Bankruptcy Act. It also entitles the grower to shall we say, a protection of a trust up to the sum of \$5,000 per creditor, but counsel from the Department of Justice was not able to tell me whether the Crown had given up its preferred position with regard to income tax deductions, unemployment insurance deductions, Canada Pension Plan deductions. Presumably the Crown has now by setting up the priority under Clause 88 (5) (b) of the Bank Act.

The CHAIRMAN: You mean only with respect to the rights of the bank?

Mr. LAMBERT: But under the Bankruptcy Act—I forget, I think it is section 95 or 96 of the Bankruptcy Act; I am quoting from memory here, the secured creditor has first claim and the Crown comes in only under the second category of priority claims. It sits in there with wages for three months and these unemployment insurance and income tax and Canada Pension fund deductions. I wonder if Dr. Ziegel considered this aspect.

Mr. ZIEGEL: Well, Mr. Chairman, if I may take the last point first, the answer is yes, not exhaustively, I hasten to add, but I have given it some thought. As I read clause 88 (5)(b) it creates a special rule that presumably would operate in bankruptcy in derogation from the order of priorities set forth in section 90 odd of the Bankruptcy Act. We, therefore, have this situation, vis-à-vis the other unsecured creditors, the bank would rely on the provision in the Bankruptcy Act which says that secured creditors might have priority but are entitled to withdraw from the debt after those which have it secured in their favour. Then you

go over to clause 88 (5) (b) and you see that it says as between the bank and the wage earners and now the growers, those two categories only have priority with respect to those particular assets which the bank has secured. It is a somewhat unusual provision, I agree, Mr. Lambert, and I am merely reflecting an impression that I formed in my own mind as to the possible way in which a court would resolve the apparent conflict between the provisions in the Bankruptcy Act and the provisions in the banking act.

As to your two other points, the conflict I suggest in clauses 75 and 88 occurred in the wording of the two clauses. Clause 75 (1) (c) says that the bank may take security on anything and then clause 88 says the banks "may" take security loans on the following. Now, the opening words of clause 88 make sense because when clause 88 was first adopted in 1890 the banks were not permitted to take security on any type of goods. Therefore, when parliament says the banks "may" take the security set out in clause 88, they were really indicating an exception from the general prohibition. Now clause 75 (1) (c) has turned this all inside out. It now follows the premise the banks may take everything as security unless we provide otherwise, and therefore, clause 88 as I say, appears to give a conflicting impression, accidentally no doubt. But this is a relatively minor point and I think it can be taken care of by amending the opening words of clause 88 so as to say without prejudice to the provisions of clause 75 (1) (c) the banks may take the securities listed in this section.

As to your wider question—should clause 88 be retained?—I make it clear, and I do not think that we differ really at all, that so long as the provincial legislation is antiquated, and much of it is, we should retain clause 88. The point I was trying to make is that the provinces are now moving into a more modern era and the federal government should assist this process because both levels of government have an equal interest in a modern system of security in personal property. They have an equal system in trying to rationalize and modernize this very complicated field of law and it would be a great pity if the federal government did not avail itself of this opportunity to try to bring about an integration of the increasingly complex rules that now govern this branch of the law. This is really the burden of my observation.

Mr. LAMBERT: Might I just make one more comment and then I will yield to someone else. With regard to the point you made about the directors, and I know I am upsetting the Chairman's priorities here, I think you will find in the proposed act, and I do not think that there was any difference in the old act, there is a provision for the so-called lesser holdings for 25 per cent of the directors. Clause 18 (2) has a proviso that says:

...except that in the case of not more than one-quarter of the directors the minimum requirements with respect to holdings of stocks in paragraphs (a), (b) and (c)...

And that is for the capitalization of \$1 million, \$2 million and \$3 million or more—

...shall be reduced to \$1,500, \$2,000 and \$2,500.

In other words, we have 50 per cent directors in so far as 25 per cent in number is concerned. Whether this meets your—

The CHAIRMAN: What clause were you referring to specifically?

Mr. LAMBERT: Clause 18 (2) at the top of page 14.

This may go part way to meeting your observations, Dr. Ziegel; it may not be sufficient.

Mr. ZIEGEL: It may not be because in the light of current market prices, Mr. Lambert, I think you will still find that a director would have to invest at least \$5,000 to qualify himself as a shareholder. What is more, he has no guarantee that he will be included in this one quarter that is subject to this reduced qualification.

Mr. LAMBERT: That is so.

Mr. ZIEGEL: What I am saying is, let us be realistic. Do we want to have a large shareholding because we think there is a guarantee of probity, or do we want to have a large shareholding because it has become a status symbol. I think it has become really more a status symbol than as any meaningful guarantee that your directors are going to be men of probity. I make this point that more directors of banks today are businessmen; they are not bankers. They have nothing to do with the day to day operations of the banks; that is rightly left in the hands of the management. They are there to provide a good business image for the banks and to give them useful contact with the business community. I do not object to this; this is perfectly proper. What I am saying is since you are really building images, how about recognizing the fact that you do a very substantial part of your business with elements in the community other than businessmen.

Mr. LAMBERT: Would this also include in the 48 per cent of non-business holdings in bank deposits all the moneys held on behalf of governments at the three levels and that you would have government officials entitled to be named to the board of directors?

Mr. ZIEGEL: No, I said there are political problems there and I am not seeking some arithmetical apportionment to directors. I want, if you will, at least a token recognition of the semi-public status of our banks because this is, after all, why we regulate them by special act of parliament and secondly, of the fact that they look to business, to all segments of the community.

The CHAIRMAN: I suppose you could also say, doctor, that with respect to the governments that in a sense the federal government is pretty close to every bank's board of directors through the Inspector General of Banking and the Governor of the Bank of Canada, in a sense.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Just in one way.

The CHAIRMAN: Just in one sense, yes.

Mr. LAMBERT: I would like to put in an observation. Banks, I think, of all corporations in Canada, make the most monthly, semi-annual and annual returns that any corporation has to ever make.

The CHAIRMAN: That is why I made that observation.

Mr. GILBERT: Mr. Chairman, they are not close in the area of decision making.

The CHAIRMAN: No, I am not suggesting that. In fact, I gather because of your reference to the management of a bank is by bankers that you do not think



banking has reached the point where you think it is too important to be left to the bankers?

Mr. ZIEGEL: It is a challenging question. I must take note of it.

The CHAIRMAN: That is a very shrewd answer.

Mr. ZIEGEL: Thank you, Mr. Chairman.

The CHAIRMAN: Thank you. Do we have any further questions on the general area of security, and so on?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Of security?

The CHAIRMAN: We may as well—this may be too technical.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I yield to my legal friend.

Mr. GILBERT: Mr. Chairman, I am very much impressed with the section that Dr. Ziegel has presented with regard to security provisions and I am just wondering if perchance amendments will be forthcoming if we could get from Mr. Elderkin some of this views with regard to these sections because, from what I understand, he participated in the drafting and I think he could probably make a useful contribution with regard to the suggestion.

The CHAIRMAN: I personally feel your suggestion is very sound. We are in a bit of a dilemma here. Our time is somewhat limited and we do not have the same opportunity to have Dr. Ziegel with us on an almost daily basis as we have with respect to Mr. Elderkin. Perhaps we might invite him to take note of Dr. Ziegel's brief and his further comments and then on another occasion when we have counsel from the Department of Justice with us we might explore this area. Perhaps, in any event, even if we had more time, it would be unfair to Mr. Elderkin to expect him to deal on the spur of the moment, almost, with these rather penetrating observations of Dr. Ziegel.

Mr. GILBERT: Yes, I agree with you, Mr. Chairman, and all I am asking is for Mr. Elderkin to take note and to assist us.

Mr. ZIEGEL: Mr. Chairman, might I make an intervention at this point to place on record two other observations concerning clause 38 which I overlooked in my initial presentation.

One concerns the place of filing of the notice the banks are required to file under clause 89, I think it is. At the moment they file this notice with the local office of the Bank of Canada. Unfortunately, most businessmen are not aware that this is the place of filing and, frequently, as Mr. Fulton pointed out at an earlier session of the Committee, the responsible agency fails to make a search in the office for bank liens. Mr. Fulton suggested that this problem could be partly met by requiring the banks to file a copy of the notice in a provincial central office in which other security agreements are filed. I think this suggestion has much merit, Mr. Chairman, and if I may I would like to recommend it for serious consideration. I think one could adopt a section dealing with the registration of the notice of intention saying something like this, that a form of order in council be made with respect to a particular province that the banks shall be required to file a copy of the notice of intention at such and such a place. This would not involve banks in any substantial additional amount of work but it would facilitate those who are responsible for ascertaining the securities given by businessmen.

The other observation I have concerns the contents of the notice which the bank has to file. It is an extremely simple form; indeed, it is one of the most attractive features of clause 88 from the point of view of the banks. All they do is file a new form saying notice is hereby given that Mr. X or X company limited intends to give clause 88 security to such and such bank. The trouble is that this tells the person who is searching the record very little about the type of security that has been given by the borrower. When clause 88 was first adopted in 1890 it was not difficult because at that time the type of collateral that could be given was so limited—it was restricted generally to inventory—that the moment the searcher saw such a notice he would realize that this must relate to inventory. Today, however, there are so many different types of collateral by so many different types of persons that can be given under clause 88 that the notice becomes meaningless.

Take for example the case of a farmer. Now, under clause 88, a farmer could give as security the following collateral; a security on crop, a security on seed grain or seed potatoes; a security on fertilizers and crops grown with it; a security on binder twine and crop that is used with it; a security on livestock, on agricultural implements, on installation of agricultural equipment, a farm electric system and finally another item, which I do not think they have noted completely.

In other words, there are no less than at least half a dozen different forms of collateral that the farmer may give. Now, what information does the notice of intention, filed with respect to a farmer, give to a fair party. I submit it gives very little information. It means that the third party has to go to the bank to find out what the notice of intention exactly related to.

The provincial requirement is far more exacting. They usually require the document filed to give complete information of the collateral so that it may be easily and readily identified. That goes a little too far in the opposite direction. They only need to meet the point and I would suggest that the notice to be filed should be amended just to require the bank to give a little more information about the collateral involved than they are now required to give. If for example, the farmer is only giving livestock as security, then I think the notice could say that the security given shall be livestock, or whatever the case may be.

The CHAIRMAN: Thank you, doctor, for this further point.

Are there any other questions on the security section of Dr. Ziegel's brief?

Mr. GILBERT: Mr. Chairman, this is just informational, but if we assume that clause 88 is not necessary because of clause 75, does that wipe out a good number of the definition sections in Clause 1?

Mr. ZIEGEL: Well, if you did decide to delete clause 88—do not misunderstand me, I think I would become the best hated man in Canada as far as the banks are concerned, if I went on record as suggesting we should delete clause 88 now; I am not suggesting that—what I am saying is that if and when the provinces bring their legislation up to date, rationalize it in such a way that the bank can take security as easily and as simply under a provincial law as they now can take under clause 88, then clause 88 should be put into limbo so far as those particular provinces are concerned.

Mr. GILBERT: I see.

Mr. ZIEGEL: I added, there are in fact, a goodly number of our provinces who are now taking serious steps to modernize their legislation in this area, and I think it would be most desirable for the federal government to encourage and assist this process as far as they can.

The CHAIRMAN: Thank you, Mr. Gilbert.

(Translation)

Have you finished your questions on securities?

Mr. LATULIPPE: I have listened with a great deal of attention to what the witnesses had to say. I do feel that all that he asks for, all that he proposes, all these things are fairly good ideas indeed. All these would allow our banks to make loans but I think it will be admitted that the present system, as proposed by our distinguished witness, is extremely complicated. All this is really designed to produce things to buy dollars, whereas what we need, really, is a monetary system which would produce dollars to buy things. That, Mr. Chairman, is the weakness of that system which has always been fostered over the centuries. It is certainly not designed to help the people. It is a system designed to exploit the people to the "nth" degree. With all due respect I feel I have to say that the tail is wagging the dog at this point.

But no real improvement is being proposed by these people who know the banking system. All these things are designed to oppress the people further.

The CHAIRMAN: I do not think that the witness should really answer your interesting remarks. He is a law professor—he is not a professor of economics or social science. I may say though that his work was designed to explain the rules which are at the basis of the present system. If any members of the Committee are not in accordance with the present system, they may well propose broad changes. But it would not be within the framework of our present discussion to ask our witness whether he shares your views or not on the advisability of changing the system. We should remind ourselves that he is a professor of law and that he deals with the system as it is. But the witness will have taken note of your intervention along with the other members of this Committee and we will certainly take into account your very interesting ideas.

Mr. LATULIPPE: I know that you do your best under the present system. It does seem to me that law professors should have other improvements to suggest. All these things are designed to oppress the people even further.

The CHAIRMAN: Perhaps we should think of our witness—

(English)

Are you in agreement with Mr. Latulippe that the basic effect of the system is reflected by the fact that it exploits the population? Perhaps this could be a take-off point for some brief comment on your part.

Mr. ZIEGEL: I was going to say, Mr. Chairman, that if a law professor were entitled to express an opinion, or cultivate opinions on economic questions he would be entitled to a double salary. My university is not in a sufficient financial state to allow—



The CHAIRMAN: Thank you very much, doctor. Mind you, you realize that double the salary you get as a witness before this Committee means nothing one way or another.

May I very briefly ask you to note a thought I have about your comment about clause 88(5) I believe. I will not attempt to enter into a lengthy exchange at this time because I want to permit the members of the Committee to have some period of time to make comments on other parts of interest to them; but I point out to you that the area of this problem with which I am most familiar, is that of the farmer growing cash crops for the canner. As far as I am aware, there is no real need for the bank to have notice of what the farmer is going to do by way of selling to the processor, because the way the system works is this: the field man of the processor goes out in the spring of the year and tries to sign up as many farmers as possible to a commitment to grow a certain quantity of crop. The contract is signed and I am pretty sure that the processor then takes the contract to the bank and it is on the strength of the contract the bank makes a loan. So the system involved is such that it would be most unusual if the bank was not pretty well aware from the beginning, of the extent of farmer participation in the production process. I just want you to perhaps take that into account in your further consideration of the matter.

A further observation is that in previous testimony before the old banking and commerce committee which led to this proposed amendment, the banks admitted more or less that of the total volume of lending in clause 88 losses in processor bankruptcies were a minuscule proportion and the whole thing is a very profitable part of their business. I expressed the doubt—which I still have—in view of the profitability of this type of lending that banks would really be that reluctant to lend even to small processors where they have a very simple solution: all they would have to do would be to put the processor's name and the farmer's name on the cheque or something to that effect and they would be pretty sure that the farmer got his share so that if there was a later bankruptcy the claim of the farmer had already been taken care of.

I just leave that with you.

Mr. ZIEGEL: Well I must admit that I have no detailed knowledge of financing arrangements in the agricultural field, and I defer obviously to your personal knowledge in the area, but I think we must recognize the greater the number of priority claims that the bank may encounter in the taking of security, the more careful, the more circumspect it is going to become in the taking of security. It must be so in the nature of things. On an average small size loan the bank makes a profit only of perhaps one half of one per cent and if the risk of loss becomes substantial, I would think it is almost the responsibility of the bank manager to refuse the loan. The marginal profit is not sufficiently high to enable the bank to take large risks. We cannot have it both ways. We cannot, on the one hand, insist on the bank operating at the lowest possible rate of return and, on the other, expect them to take above average risks; so I say by enlarging the number of priorities over the claim you are coming close to that situation.

The CHAIRMAN: I just wanted to suggest again, we could perhaps devote a considerable period, just to look into this matter, but it would seem to me that the determination of the risk, using the type of criteria you use in the retail business, for example, where they grade the losses in particular categories of

borrowers or customers, would indicate a very small possibility of loss in this, I think that really the question of enlargement of risk should be decided in all logic—perhaps not in all logic, but perhaps in some useful way—before you begin looking at the number of people among whom you have to divide things if there is a loss, but the possibility of the loss itself in the sense of a failure of the customer is a prior consideration. In other words, there really should be two steps: you first should ask, what is the possibility of this firm, or this class of firm, failing? Now if there is little possibility of either the firm or the class of firm failing, then the question of among how many people you are going to have to divide what is left is not as relevant as it would otherwise be.

I just throw this at you for your further study of this problem and we are going to hear from the Federation of Agriculture, I think, after Christmas and we may go into it further.

Now, are there any further comments or questions on the very interesting proposals of Dr. Ziegel in the area of wider representation on the boards of directors of banks.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I notice, Dr. Ziegel, that in the final sentence on page 7 you have an insert in brackets regarding the possible nature of the additional directors. I wondered, as soon as I saw that, whether you suddenly had an excess of caution when you put that in and I wondered why you did it. I think your idea of a broader representation is an excellent one and I cannot think of any other way in which the general customer of banks could be better represented than by representations of public authority.

As I recall it, from the reading I have done on the matter with regard to the developments in France under the Commissariat du Plan de Jean Monnet, after the second world war there were legal provisions there whereby the government of France appointed directors to, I think, all the banks in France, directors not with limited voting powers but with power of veto and I am not sure, you may possibly know, whether this still is in effect or not. I wonder if directors with full voting powers—possibly not with power of veto—might not better serve the purpose you have in mind.

Mr. ZIEGEL: Mr. Cameron, I was not beset by an excess of caution. I introduced the word in parenthesis because I appreciated not merely the novelty of my proposal, but also its collision with traditional corporate law principles. Directors, you see, are normally elected. My proposal would confer powers of appointment on the minister, I felt this was so much at variance with the elective principle of directorship that one should recognize this departure by putting the appointed directors in a special category. Let me add I would hope that the minister would never have to exercise the power. It would not only be an invidious power to exercise, but it might also become an undesirable instrument of patronage, and that is the last thing I would want to see. I think it should merely be the carrot and the big stick, or notice, if you will, to the banks that they should become more broadly based in their directorship, and if they were not willing to see the light of day by themselves then the minister would have to guide them. I have no illusions that the presence of directors representing other parts of the community is not necessarily going to swing votes one way or the other. It would depend on the number of directors you have.



I have no illusions either, Mr. Cameron, about the importance of directors in the day-to-day operations. I think this is insignificant, because, for one thing, banks are so circumscribed, in so many of their operations, by the Bank Act that they have little opportunity for innovation. Mind you, one of the reasons why I would like to see wider representation is that I think there is too much inbreeding among directorships. Big businessmen do not know how the ordinary depositor or borrower thinks or lives. I think a wider representation would explain some of the every-day reactions and experiences and perhaps bring forward suggestions which would make bank operations more useful and perhaps more practical to the every-day Canadian than they are now. An example which occurs to me is in respect to the opening hours of banks. Another example would be that had they had consumer representatives on the boards they might well have been willing to enter the consumer loan field earlier than they did.

These are merely possibilities, and I am not saying that this is necessarily the case.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would you not agree, Professor Ziegel, to be realistic, as you suggested some time ago, that there would be really little possibility of such a person as you have described actually being elected to the board of directors of a bank except as a "front" man for the establishment of the bank?

Mr. ZIEGEL: This is a very interesting question. It is well known that in all the big corporations directors are nominated by management. Management does not by any means mean the majority of shareholders; it means those shareholders who have a special block of shares and who are able to dominate meetings.

It is quite conceivable, as you suggest, that bank management, in order to comply with the spirit of the proposed provisions, would put forward one or two "front" men, but there is another alternative, Mr. Cameron. I think that if banks had much more democratic meetings, in the way I suggested, by drastically altering the use of proxy votes, at least there would be an opportunity for ordinary shareholders to try to contact a sufficient number of shareholders to have themselves put forward as nominees. I think this move would be assisted if, for example, we also considered the introduction of a cumulative voting system. That would mean that the shareholder could put all his votes in favour of one director instead of the 40 odd among whom he has to divide them now.

I did not intend to develop my suggestions at any length, in the few lines at page 7 of my brief. I was more concerned about establishing some sort of principles. Obviously much more work would have to be done on the details.

The CHAIRMAN: I was interested to have you finally put forward the cumulative voting proposal. It is another alternative to, or an extension of, what I think is the very constructive concept involved in your section 3.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Is there not another concept that perhaps we should keep, in mind, Dr. Ziegel? Largely because of the development of banks and what we envisage as their future development—which has come up again and again in the hearings today and in Dr. Neufeld's presentation—that the chartered banks will assume a larger and larger role in our economy, do you not think it is desirable to have not merely the chance of getting some ordinary citizens on to the board of directors, but having an actual



representative of the Canadian people there? Although it may be true that directors have little or nothing to do with the operation of the bank, nevertheless a director there as a watchdog for the Canadian public would have access to information that the non-director would not have. Is that true?

Mr. ZIEGEL: He might well have access, Mr. Cameron, but I think he might also have a very real conflict of interest between the two parties. For this reason, as well as others, I am by no means persuaded that direct government representation is the answer. We do have very important institutions, such as the Bank of Canada, where the government makes nominations, but the directors are, in no sense, nominees of the government, nor are they directly responsible to the government.

I think that even in corporations it is very important to retain the principle of the independence of the members so that they will genuinely follow the basic policy of the institution they serve rather than make decisions that may look politically expedient.

If it were necessary for the minister to appoint representatives, or a board of directors, I think it would be wise to observe the same principle, namely, that the person who is appointed be in no sense responsible to the government; that he be wholly independent, and that he follow his own conscience and good judgment and not those of anyone else.

Extending this idea, I see no reason, for example, why a bank should not say: "We have dealings with a very large number of wage earners. Why not have a union member on a the board of directors." I think this would be an excellent idea, but I would be most unhappy if I thought the union member were there in order to tout union policies. I think that once he is appointed, or elected, as the case may be, he should use his own best judgment with respect to decisions that come before the board of directors.

Mr. CAMERON: (*Nanaimo-Cowichan-The Islands*): You make the suggestion yourself that the Minister of Finance appoint a director. Could he not be appointed perhaps in the way that we appoint a number of our public officials, such as the Auditor General and some others who are directly responsible to Parliament and who are not responsible to the government—responsible to the people's representatives and not obliged to follow government policy—in who are there merely as watchdogs for the people of Canada? Would it not be possible to devise a method of appointment of a director who would represent the Parliament and the people of Canada in that way?

Mr. ZIEGEL: Yes; but you must not forget Mr. Cameron, that you are not dealing with a single institution here. You are dealing with at least 8, and prospectively 10, different and competing institutions. Moreover, the designated representatives would have to deal with many commercial considerations. I think this would complicate the picture considerably, and it may create difficulties if the Government of Canada suddenly found itself having to designate certain representatives on 8 different institutions. It is for this reason that the principle which I am trying to develop would have to be given much more careful consideration in any practical implementation.

The CHAIRMAN: Are there any further questions?

Mr. MORE (*Regina City*): Dr. Ziegel, I was wondering about your suggestion that the Minister of Finance be given a special power in this connection. Do you really think that any Minister of Finance would want to be put in this position?

Mr. ZIEGEL: Well, I suggested—

Mr. MORE (*Regina City*): How broadly should he interpret the lack of representation on a bank's board of directors, with respect to specific groups within our community?

Mr. ZIEGEL: That is another of the important questions that would have to be considered in drafting the new provisions. So far as the appointed minister is concerned, I suggested the Minister of Finance because he is responsible to Parliament for the general administration of the Bank Act. I would have no objection if it were some other minister, or indeed if it were not a minister at all, but some council, or other group of individuals. Let me stress again, if I may—

Mr. MORE (*Regina City*): A finance council?

Mr. ZIEGEL: Yes; I am not anxious at all that the minister should have to exercise this power. I think it should be a reserved power, to be exercised if, indeed, the banks refuse to co-operate. My hope would be that Parliament having made it clear, both in the spirit and the letter of the law, that a much broader representation on boards of directors was desirable, the banks would fall in line.

Clause 91 is a good analysis. As I indicated earlier, in law there is nothing to prevent the banks from flouting the 6 per cent ceiling. In practice they have not done it outside the special area of consumer loans, because they knew what the feeling of Parliament was and they knew what public reaction would be. In this instance public opinion was a more powerful factor in preventing the banks from exploiting legal loopholes than the provisions of the law itself. My hope would be that something similar would happen with respect to direct representation.

I might add that I have occasion recently to mention my suggestion to the president of one of our largest banks, and he did not take at all unkindly to my suggestion that the banks should broaden their bases of representation. His answer was: "Who do you suggest?" I must add that I was too modest to suggest to him who immediately came to mind; but as I say—

Mr. MORE (*Regina City*): I suppose that by this suggestion you are saying that, in view of the liabilities which are inherent in being a shareholder, the bank would not limit the appointment that a minister could make under this clause? In the areas of community representation that you are suggesting, would not the people who might be chosen be reluctant to become a shareholder and accept these liabilities?

Mr. ZIEGEL: First of all, you would have to decide whether they would be shareholders at all. This is where we run into the problem I mentioned in connection with Mr. Cameron's question, that you are, in a sense, mixing two different concepts, namely, the appointed director and the elected director. Theoretically, you could have a scheme where a certain number of directors are elected by shareholders and a certain number are elected by non-shareholders; or, again, where a certain number are appointed by some outside body, or council. These details clearly would have to be worked out, but they are not novel.

We know that in many areas of the world you have had systems of government where a certain number of representatives have been elected and a certain number have been appointed. In Canada, we have various spheres of government and there is nothing novel about that; but I do agree with you that these various problems would have to be given careful consideration in the ultimate phrasing of whatever provisions were adopted.

Mr. MORE (*Regina City*): Your view is that the board of directors could be expanded, but that the requirement that they be shareholders should not necessarily be maintained?

Mr. ZIEGEL: First of all, as I have said, the present requirement, which amounts, in effect, to a director's, having to hold as much as \$35,000 worth of stock, is wholly unrealistic and undemocratic. A man should not be denied the right to be elected director simply because he is not fortunate enough to be a millionaire. In any event, I suggest that the qualification requirements should be substantially reduced, or even eliminated altogether. It seems to me that if you accept my suggestion that the present qualification requirements are, in any event, obsolete and in need of modernization, then the second problem of what qualifications are to be imposed upon these new appointees becomes much simpler to solve.

Mr. MORE (*Regina City*): I was interested in your use of the word "in-breeding" in referring to directorships. It seems to me, in my limited knowledge, that biologically, or genetically, there is a period when this improves the quality of the product. Do you suggest that that period is passed in the case of bank directors?

Mr. ZIEGEL: I must confess that my recollection of the law of genetics is somewhat different from yours.

Mr. MORE (*Regina City*): Are you acquainted with the restriction that was inserted in the Bank of British Columbia bill on the appointment of government people?

Mr. ZIEGEL: I have read about it, but I must confess that I have not studied the bill.

Mr. MORE (*Regina City*): Therefore, you cannot say whether, in general, you agree or disagree with it?

Mr. ZIEGEL: I would rather not comment.

The CHAIRMAN: In any event, that bill is not before us at this time.

Mr. MORE (*Regina City*): Very well.

The CHAIRMAN: Perhaps we should continue for a brief period in case there are further questions which members may have on the remaining sections of Dr. Ziegel's brief.

First of all, there are his views on "Disclosure Requirements in Personal Savings Accounts." Are there any further questions on this section of his brief?

I might mention, with respect to prominently displaying interest rates in the precincts of banks, that the trust companies seem to be able to do it without causing any damage to any one.



I also want to say that while Dr. Ziegel was presenting this portion of his brief I saw a member of the audience—I will not identify him—take out his bank pass books and study them. I suppose, if necessary, we could call the individual as an expert witness. Perhaps I should say, for the record, that he is a member of the press, and it would be a novel experience for both of us. The fact that this individual was interested enough to look at his pass book shows that this is potentially an area of great interest.

If there are no further comments on that section I will ask if there are further comments on Dr. Ziegel's views in the portion of the brief entitled "Disclosure of the True Cost of Bank Loans."?

Mr. GILBERT: Mr. Chairman, I would like to ask Dr. Ziegel for his views on the delay in the timing. He said that he had reservations about the timing of federal legislation because of provincial acts that have come, or are coming, into effect. What, if any, is the jurisdiction of the provinces in this matter?

Mr. ZIEGEL: The present legal position would appear to be that jurisdiction is divided between two levels of government. This arises because of the narrow meaning which the law has hitherto placed upon the word "interest". Subsection (19) of section 1 of the British North America Act confers exclusive jurisdiction on the federal government to regulate matters of interest. This is the basis of federal jurisdiction in the small loans sphere.

There are decisions, mainly American and English—and also some Canadian ones—which say that first of all a finance charge levied by a retailer, or other seller, in consideration of extending credit, is not interest in the legal sense. Secondly, we have the recent decision of the Supreme Court of Canada in the Barfried case, saying that even in a loan those elements outside interest—whatever that may mean—do not constitute interest. It sounds like a tautology, but I am afraid this is exactly what the court said—and therefore are not subject to federal legislation. The result is there is a very considerable sphere in which the provinces have to restrict them.

My point about timing was directed to Professor Neufeld's suggestion that the disclosure provision should be extended to all class of loans and not be restricted to consumer loans. What I said was that the existing provincial legislation dealing with disclosure questions is generally restricted to consumer transactions and that if the federal government now decided that they were going to apply the principle to all lending transactions there would be an apparent inconsistency between the federal and provincial legislation. It might take some time to resolve this inconsistency. We already have had, I think, more than sufficient delay, and I am willing to forgo, for the moment, the extension of the disclosure principle to all types of loans, for the sake of seeing some legislation introduced now at least to protect the consumer.

Mr. GILBERT: If I may take your example of appraisal expenses, in a mortgage loan this expense is usually allocated to the legal expenses, and the banks usually retain a firm of lawyers and it is part of their charge.

Mr. ZIEGEL: That is right; and this is what creates difficulty. The same problem arises under the Small Loans Act. If a small loan company retains a lawyer to draw up a chattel mortgage they will have to pay for this out of their own pocket, and they could not require the borrower to pay this amount over and above the permitted levels of the Small Loans Act. But because the small

companies do not use outside lawyers and because they do not have any special expenses, this problem does not worry them. If, however, you are entering the sphere of big commercial loans, where expenses can sometimes run into thousands of dollars—for example, an issue of bonds or debentures—if enough money is involved the legal and other fees can be very substantial indeed. I would say that in those circumstances banks are certainly not prepared to absorb those expenses, and if they have to include them in their reckoning of the interest rate this might present a somewhat distorted picture. I am merely offering a tentative thought, not a final one. It is certainly something we will want to think about a little more.

I do not think we have to be worried about protecting the huge commercial companies. They are highly sophisticated; they have vice-presidents in charge of financial affairs; and they are very capable of working out the cost of a loan themselves. We are concerned about the position of the small borrower, or the consumer, who is confronted by a bewildering mass of different charges by different institutions. He is the one who needs the common yardstick. He is the one who most urgently needs our protection.

Mr. GILBERT: Thank you very much, Dr. Ziegel.

Mr. LAMBERT: For the ordinary individual, who is going to borrow \$15,000 to \$20,000 on a house mortgage, with varying scales of legal fees across the country, surely you are not going to suggest that there be uniformity so that they will be hemmed in by some form of statutory strait-jacket.

Mr. ZIEGEL: Oh, indeed not.

Mr. LAMBERT: I can tell you that the legal fees in the province of Alberta, for instance, with regard to mortgages are perhaps only a third of those in Ontario. Therefore, the Ontario borrower, under your thesis, would be charged at a much higher rate of interest than he would be in other provinces. I cannot agree with this. I think there is interest and there are these additional charges.

Mr. ZIEGEL: Oh, no; that, with respect, would completely demolish the value of any disclosure requirements. This was the very essence of the definition of the term "cost of loan" in the Small Loans Act, because what had happened was this: Under the earlier interest acts small companies had successfully evaded the interest ceilings by exacting charges under different guises. To prevent this you have to adopt an all-embracing definition of the cost of the loan. I think that if you are going to have a disclosure requirement you must adopt a similar principle otherwise the legislation will not be worth the paper it is printed on.

The problem of rate is a different one. Namely, should the disclosure principle be applied to real mortgages? If my recollection serves me correctly, it has not hitherto been applied to real mortgages; it has been applied only to the consumer loans, either for personal use or for goods.

Mr. LAMBERT: I have had years of experience in preparing the statements under the then-existing Alberta act which, I think, came in about 1954. It required a statement in statutory form showing the cash value of the goods turned in in exchange, the amount of any registration charge, of any, shall we say, credit report charges and of any insurance. It was all set out in tabular form in dollars and cents. The purchaser saw that. He knew what he was buying.



Mr. ZIEGEL: With respect, it did not give him the comparative yardstick that he needed. He might know that I was charging so many dollars by way of expenses and finance charges, but how was he to compare this with the bank around the corner that said: "You pay us 6 per cent, and you pay a service charge of \$1.75 and then there is a \$2.00 registration fee, and, let me see, another \$2.00 for insurance." If he went around to a small loan company and said: "How much would you charge me for borrowing \$1,500 to buy a car?" they would give him a different list of charges entirely. The average consumer is not a mathematician, and he would be completely confused and befuddled.

The object of the disclosure of profit and I mean by that disclosure in terms of effective annual interest rates, is to give the borrower a common denominator so that regardless of where he goes to buy his goods, or borrow the purchase money, he has an easy way of comparing the cost of the different institutions. That is the object of the exercise. Dollars and cents would not accomplish this.

Mr. LAMBERT: My feeling is that the consumer wants to know how many dollars and cents he is going to be paying, and whether it is 8.6 per cent or 8.7 per cent in the total matters little to him.

Mr. ZIEGEL: Than from the consumer?

Mr. LAMBERT: The man who is buying a TV set is interested in how many monthly payments of how much he is going to be making.

The CHAIRMAN: He is also often quite surprised to find out that he may be paying 20 per cent per annum on the contributory rate of interest.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then he could borrow the money from the bank and pay cash.

Mr. LAMBERT: If he knows how much money he is paying towards interest and so forth, and how it is allocated, he can work out the percentage.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): A lot of people who buy TV sets cannot do that.

Mr. LAMBERT: May I say that under the Alberta act, after extensive hearings it was determined that it was preferable from the consumer's point of view, to show it that way rather than as some form of interest rate which, in essence, can be meaningless because what is 8 per cent of apples is not 8 per cent of oranges.

Mr. ZIEGEL: With great respect, sir, here I must vigorously dissent.

We held a conference in Saskatchewan early this year on consumer credit, and we had a most distinguished panel discussing the problem of disclosure requirements and consumer credit agreements. The overwhelming majority of members of that panel were in favour of the disclosure of requirements, outside the business interest. One of our panelists was Mr Aalborg, the provincial treasurer of Alberta. If my recollection serves me correctly, he advised the conference that it was the intention of the Alberta government to proceed with the implementation of that section of the Credit and Loan Agreements Act that dealt with the disclosure of the cost of credit in terms of an effective rate of interest. Therefore, I think that even in Alberta they have by no means abandoned the principle which we now hope to see implemented in the federal Bank Act.



Mr. GILBERT: Mr. Chairman, this is also a recommendation of the Porter Commission.

Mr. ZIEGEL: It is, indeed. Every committee in Canada which has investigated the question has supported the principle. The select committee in Ontario did, and it is now being adopted in the Ontario Consumer Protection Act. In Nova Scotia you had a very detailed, careful study, I think, by Mr. Arthur Moreira, and he came to the same conclusion without any difficulty.

In Canada, at any rate, I think there is a uniform consensus among those independent legislative bodies that have had an opportunity to look into the question.

The CHAIRMAN: We have had a useful exchange in this important area and if there are no further questions on the remaining section of Dr. Ziegel's brief, I suggest that we thank Dr. Ziegel for appearing before us today and for making a very useful contribution to our work, especially in that he has brought forward some ideas on areas of our order of reference which have not really been touched on as yet.

With that comment I would like to declare this—

Mr. MORE (*Regina City*): Sir, before you adjourn, and so that it will be official, I want to raise the question that your colleague raised earlier in the day, about proposed sittings on Tuesday.

The CHAIRMAN: Yes.

Mr. MORE (*Regina City*): We had a night sitting on Tuesday with a very important witness and we have completed it now at 10.15, and outside of yourself there have been no government members participating in the sitting whatsoever.

The CHAIRMAN: It may be a tribute to me; I do not know.

Mr. MORE (*Regina City*): I want to raise it, because there has, perhaps, been a little foot work today and we, as members of the opposition, feel we have the same obligations to the opposition as government members may feel they have to the government. Perhaps you are not even aware of what went on, to a degree at least.

I think that in cases like this, at least, there should be some responsibility to cancel a sitting. I am wondering about Tuesday. Are we going to have a night sitting, with three sittings on Tuesday? Are we going to be able to have Committee representation at these sittings? I think it is very important.

The CHAIRMAN: Thank you for raising this issue. I should state for the record that I am personally not aware of any arrangements on the part of government supporters. I have been devoting my attention today almost entirely to the work of this Committee, and I might say that so far as I am concerned I expected to have supporters of the government, in addition to myself, present this evening.

With respect to Committee sessions on Tuesday, all I can say is that the steering committee recommended to the full Committee that we meet on Tuesday, and we agreed to invite certain witnesses to appear.

I am not in a position to comment on what work the House may be doing on that day but I would suggest to those present and to those not present that we

are working toward a certain deadline—not so much as a Committee but as a parliament—in the matter of the most recent extension of the Bank Act, and every time the opportunity for a meeting is lost, even though it may be for what many consider to be a good reason, it puts additional pressure on us to complete our work. I am sure that we would not want to be put in the position, if we can help it, of dealing with any of these matters without having the fullest opportunity to consider them, because although there have been recommendations made that this be done more often than every 10 years we cannot be sure this will happen; and we have some obligation both to Parliament and to the country to work expeditiously but carefully.

Mr. MORE (*Regina City*): I agree with those remarks, but I do not think the obligation should be placed almost entirely on opposition members.

The CHAIRMAN: I do not disagree with you. I can only repeat that I expected some other government supporters to be present. I want to thank those here for participating, particularly since we have such a distinguished witness with us this evening.

The best suggestion I can make is that we continue our plan to have meetings on Tuesday as scheduled. Perhaps, without saying this officially, we may decide that it will not be necessary to meet on Tuesday evening because the Canadian Credit Men's Association has only one major point to bring to our attention, and a night sitting may not be necessary. I think we will know better on Monday what things look like for the last week. Perhaps the Steering Committee should try to consult informally later in the day to consider how we should proceed.

Mr. LAMBERT: Mr. Chairman, the reason for raising this is that there was an overt move in the house at 7 o'clock tonight to try to force an all-night sitting.

The CHAIRMAN: I am not aware of it.

Mr. LAMBERT: This sort of thing depends upon the voting presence in the house at 10 o'clock, and the government members are obviously absent because—

The CHAIRMAN: If those present had informed me of this and if they had felt that we should suspend our sitting earlier this evening, I certainly would have had no objection.

Mr. LAMBERT: I would not want to be discourteous to our witness for that purpose.

The CHAIRMAN: In any event—

(*Translation*)

Mr. LATULIPPE: Would it be possible, later, after the Christmas recess, to call witnesses from Caisses Populaires, in order that we may know their views with regard to deposit insurance and other things?

The CHAIRMAN: After the holidays we will have a group with us, called "CUNA INTERNATIONAL". According to my information, they represent the entire gamut of Credit Unions and Caisses Populaires. They have already tabled

a brief with the clerk, this will provide us, I think, with an opportunity to study their ideas with regard to the Bank Act.

Mr. LATULIPPE: Thank you, Mr. Chairman.

(*English*)

The CHAIRMAN: I declare this meeting adjourned.



## APPENDIX "Y"

Submission To The  
Standing Committee of the House of Commons  
On Finance, Trade and Economic Affairs  
Regarding  
Bill C-222 An Act Respecting Banks and Banking

By E. P. Neufeld  
Department of Political Economy  
University of Toronto

The changes in Canadian banking that Bill C-222 introduces are fundamentally important, probably more important than any others introduced by legislation in this century. I strongly support the principle that seems to underlie them:—increased efficiency in the banking system through greater competition and through fewer statutory restrictions on the banks' lending and borrowing activities. Furthermore, I support a number of the specific changes themselves, although I believe that some of them should be modified. Since the changes *are* important it may be helpful for the deliberation of this Committee if I were to indicate where I believe that further thought and consideration might be justified. In order to lend substance to some of my reservations, I will offer certain general recommendations for amending Bill C-222.

My comments are divided into two parts: those dealing with the effects of proposed changes on other financial institutions; and those concerned with a number of individual items in Bill C-222.

*I Banking Legislation and Non-Bank Institutions*

1. Banks, trust companies, and loan companies

The new banking legislation will tend to increase competition by extending the banks' borrowing and lending powers into fields they do not now occupy, and by making collusion between financial institutions more difficult. The latter will be achieved by the prohibition on interest rate agreement between banks (sec. 138), by the limitations on interlocking directorships (sec. 18), and by the proposed interest rate disclosure provision, all of which I support and so need not discuss here. At the same time the reduced competition arising from the restrictions on foreign ownership of banks in Canada will at least to some extent be compensated for by the proposed licensing of agencies of foreign banks—a matter to which I will refer again.

The competitive strength of the chartered banks will be enhanced by the provisions enabling them to engage freely for the first time in their long history in conventional mortgage lending (sec. 75), by permitting them gradually to introduce a new financial instrument for raising funds—the bank debenture (sec. 77), and by eventually relieving them of the ceiling on loan charges (sec. 91).

The strengthened competitive position of the banks that these changes will make possible may be regarded as only "fair" in view of the fact that the relative size of the chartered banks has declined quite steadily over many decades—to-day amounting to perhaps one third of the assets of all financial intermediaries compared with three quarters at the time of Confederation. However the real justification for the changes does not lie in their "fairness" but rather in the strong probability that they will lead to a more efficient financial system. The benefits of that increased efficiency should accrue to the many small savers who hold at least some of their savings in bank accounts and the many borrowers who now suffer from inadequate current loan and conventional mortgage loan facilities. It is quite conceivable that the higher bank lending rates will encourage some large corporations to switch from bank loans to market issues for raising money, thereby leaving more bank accommodation for borrowers who do not have access to the capital market, and who have been paying high rates of interest to non-bank lenders. The removal of the legislative restrictions that have impeded the development of such a system is highly desirable.

But two important points must be recognized. First, to the extent that legislative restrictions on the banks have over past years encountered the growth and the development of other competing financial institutions, such as the trust companies, and loan companies, there is an obligation on the part of Parliament to ensure that the effects of their removal on other financial institutions and on the economy generally are minimized. That is, Parliament must minimize the transitional costs of the removal of such restrictions. Second, if important legislative restrictions on the banks are removed in a way that enhances their competitive position, it is vitally necessary that Parliament remove the legislative restrictions that may have impeded the growth of other competing financial institutions.

I believe present legislation deals only partially with the first point (i.e., transitional problems) and quite inadequately with the second. The principle of permitting the banks to move only gradually into debentures is a sound one (although the actual rate of increase chosen should, I believe, be changed), but it is one that should also be adopted for removal of the 6 per cent ceiling. Both bank borrowers and bank competitors should be given time to adjust to a free bank lending rate; and preferably they should be permitted to do this in times of prosperity, that is, when interest rates are high. Present legislation does not envisage this. While I discuss the matter of the bank lending rate in the next section, *the above considerations, as well as others to be noted later lead me to recommend that the 6 per cent ceiling be raised by  $\frac{1}{2}$  per cent per annum for five years after the coming into force of the new legislation, regardless of the levels of Canadian interest rates in existence at the time, after which it should be removed completely.*

Then there is the matter of perpetuating important restrictions on other financial institutions at a time when restrictions on the operations of the banks are being reduced. The new legislation accepts the principle that chartered banks should engage in conventional mortgage lending and should be permitted to issue debentures. This removes all unique advantages that legislation of the past century or more has conferred on the mortgage loan companies and, apart from fiduciary powers, that legislation over three quarters of a century has conferred on the trust companies. It is true that the amount of debentures that

the banking system is to be permitted to issue is limited. But the limitation itself can only be justified on grounds of easing transitional adjustments, and must be regarded as undesirable over the long term.

What should now be done is to enhance the potential competitive position of the trust and loan companies, and not merely by amending the legislation under which they operate. Since many trust and loan companies have developed a chequing deposit business (which in my view constitutes the basic criterion of whether a financial institution is, or is not engaged in the "banking" business), and since chartered bank lending business will now include the traditional trust company and mortgage loan company business of conventional mortgage lending, and finally since bank borrowing activity will extend to the traditional trust and loan fields of selling debentures (Guaranteed Investment Certificates essentially are debentures)—for all these reasons new legislation should aim at standardizing the rules and supervision under which the banks, trust companies and loan companies operate. *I would therefore recommend that the Bank Act be amended to enable trust companies and mortgage loan companies to become banks. More specifically, I would recommend that any trust or loan company that met certain defined (fairly stringent) financial standards should be granted a bank charter, if it wanted one, even though its present asset and liability structure is different from that stipulated by existing banking legislation.* I would envisage that after about a decade (that is, in the next decennial revision of the Bank Act), the borrowing and lending powers of existing banks would be made identical to those of the "transformed" banks.

In order to assist any trust company to make the transition to becoming a bank, I would recommend that existing banks not be permitted to enter the fiduciary business (whether through merger or otherwise) until at least the next decennial revision of the Bank Act. In other words for a ten-year period there would be, in effect, two kinds of banks under the Bank Act, while at the end of that period all chartered banks would enjoy the same powers.

Some such accommodation in the present banking legislation is, I think important. Without it the long-term competitive prospects of the loan and trust companies do not seem bright—particularly after any remaining restrictions on the volume of debentures that the banks are permitted to issue are (quite rightly) removed.

It is to be remembered that this would not be the first time that Canadian financial institutions needed to alter their character to survive, or even the first time that legislation was used to encourage such a change. The pre-confederation Savings Banks were required by legislation to transform themselves after Confederation, as in a sense were the foreign fraternal benefit societies after the turn of the century. And over the years the terminating building societies evolved into permanent mortgage loan companies (and were legally permitted to do so), many of which in the 1920's transformed themselves into trust companies—a move which was necessary for their survival and one which was made possible by legislation of the day. It would therefore be entirely within the tradition of the past if trust and loan companies were now permitted to become banks. I can see no valid objection to such a move. It would enhance competition by increasing the chances for the long-term survival of the trust and mortgage loan companies; it would permit Parliament to honour its obligation to financial institutions that have grown in the past partly because of unjustified legislative



restrictions on the banks; and it would pave the way for the development of local branches that would provide individuals with a much more adequate range of financial services than unfortunately is now the case.

In view of all these considerations, I would recommend that a special section be inserted in the Bank Act dealing with the conditions under which existing financial institutions could be given the opportunity to evolve into banks.

## 2. *Deposit Insurance*

I favour the introduction of deposit insurance for federally incorporated financial institutions that take deposits. It would improve the competitive position of smaller institutions and increase their chances to grow. However, I do not regard this approach as an adequate substitute for the approach I outlined above. That is, it is not a satisfactory substitute for enabling existing financial institutions to transform themselves into banks if they wished to do so and if they met certain defined standards.

## II *Specific Changes In The Bank Act*

I shall refer here only to those items in the Bank Bill that I think would benefit from further consideration, items on which I have been able to form an opinion with a degree of confidence.

### 1. *The 6% Interest Rate Ceiling On Bank Loans*

I favour removal of the interest rate ceiling. However, the procedure for doing so as outlined in sec. 91 subsec. (9) seems unsatisfactory for two reasons. First, it would delay removal of the ceiling almost indefinitely if high levels of economic activity were to continue, for under those circumstances short-term Government of Canada bond yields would probably remain above 4½%. Second, it would lead to an abrupt end to the ceiling whereas, as I explained earlier, a more gradual but completely certain removal would be desirable. For these reasons I favour raising the ceiling by ½% per annum for five years, and removing it entirely thereafter.

### 2. *Proposed Interest Rate Disclosure Provisions*

I would wish to emphasize my support to the intention of the Government to include interest rate disclosure provisions in the Bank Bill by saying that in the absence of such provisions it is my feeling that the ceiling on bank loan rates should not be removed. It should be noted that ignorance over the true cost of loans impairs the functioning of the capital market in much the same way as does the interest rate ceiling. Therefore removing the ceiling would remove one imperfection, but without interest rate disclosure provisions it might aggravate another.

I think it is important that all charges be included when computing the simple average annual rate of interest on bank loans. There is no economic logic in distinguishing between "interest" and "special charges", for "interest" is simply the cost of money.

### 3. *Debenture Borrowing*

I support the principle of a gradual introduction of bank debentures. However the present provisions for limiting the total amount outstanding and the annual rate of increase seem to me to be unduly restrictive. I would favour

permitting an annual increase equal to 15% of capital and rest for a period of ten years. Further increases might be considered at the next decennial revision of the Bank Act.

#### 4. *Cash reserve ratios*

The introduction of a "split" cash reserve ratio—12% for demand deposits and 4% for savings deposits—is an implicit acknowledgment of the fact that not all banks have the same relative amounts of the two kinds of deposits. If they did, one over-all cash reserve ratio would suffice, adjusted periodically to take into account any change in the relative amounts of each type of deposit in the system as a whole. However, banks vary one from another in other respects—particularly in the nature of their assets, and this the new cash ratio formula does not recognize.

It should also be understood that the *fixed* cash ratio is desirable only because it improves the predictability of the effect of Bank of Canada actions on the size of chartered bank deposits; it does not in any material way ensure the solvency of the banks or make them more efficient.

Taking these several points into account, I think that the following approach to the cash reserve ratio would be superior to the one proposed: the new legislation should require each bank to indicate annually to the Bank of Canada what it wishes its minimum cash ratio to be for one year ahead. This would enable the Bank of Canada to compute a fixed minimum cash ratio for the banking system as a whole which is useful for purposes of monetary control; it would enable each bank to decide its minimum cash ratio taking into account *all* relevant factors, not just its deposit structure; and it would make it unnecessary to determine the very difficult question (in the Canadian banking system) as to what constitutes a demand deposit and what constitutes a savings deposit. Nor would there be any harm in permitting the banks to consult with each other when deciding on individual minimum cash ratios.

#### 5. *Secondary Reserve Ratio*

The Bank Bill would place the secondary reserve ratio on a statutory basis, in place of the present informal arrangement between the banks and the Bank of Canada (Sec. 72, subsec. 3). I agree that if such a device is used it should be provided for in legislation and should not be introduced through "moral suasion".

At the same time I do not believe that the technique of a secondary reserve requirement is sufficiently effective for purposes of economic stabilization to justify imposing it on the chartered banks. I would favour that it be dropped from the Bill.

The purpose of the secondary reserve ratio presumably is to control the rate at which banks switch from liquid assets into loans. However, this will be determined by the over-all asset structure of the banks, not just by their holdings of "secondary reserve" assets. For example, at present the banks are in a position of minimum liquidity which for some months has meant that their combined holdings of cash, Government of Canada Treasury Bills, day-to-day loans, and holdings of Government of Canada bonds have remained at a level equal to about 30% of their Canadian deposit liabilities. Any significant decline in that ratio would probably be precluded by the need for the banks to maintain a satisfactory liquidity position on grounds of sound commercial banking. That

is, it is not the secondary reserve ratio that now prevents the over-all liquidity ratio from going lower. Also, in a period of easy money it will probably be the non-secondary reserve ratio assets that will rise and that will permit a future shift from liquid assets into loans. The secondary reserve ratio will not prevent it. Also, the tendency of the bank to shift out of liquid assets into loans contributes to establishing an anti-inflationary monetary policy for it assists in establishing higher interest rates. It is true, however, that in unusual circumstances an overly rapid shift of that kind might produce unsettled market conditions, but I do not see this problem as sufficiently important to justify the secondary reserve ratio.

The proposed legislation, of course, would not impose a secondary reserve ratio but rather would enable the Bank of Canada to impose it if it wished to do so. Because of this, it might be thought that objection to it is unreasonable. However since the Bank of Canada in the past has used its influence to impose the ratio, and then has used its influence to retain the device when in my view there was no justification for doing so, I am obliged to recommend that the Bank should not be given the authority to force the banks to maintain secondary reserve ratios.

It is to be noted that the proposed legislation actually extends the potential impact of the secondary reserve ratio for it would permit the Bank of Canada to vary it between 6% and 12% of Canadian deposit liabilities, in place of the fixed 7% ratio in existence at present. Any such move to increase the legislative rigidities in the banking system should be examined most carefully on its merits, particularly at a time when attempts are being made to *reduce* legislative rigidities.

#### 6. *Foreign bank agencies*

To permit foreign banks to operate agencies in Canada could mean that foreign banks would provide some competition for the Canadian banks in the large financial centers of Canada. How many Canadian dollar deposits they could attract, and so how many Canadian dollar loans they could make cannot be known in advance. At present the Canadian chartered banks' U.S. deposit liabilities owned by U.S. residents amount to about 5% of the banks' total Canadian deposit liabilities. If U.S. banks operated agencies in Canada it may be that they would accumulate a similar amount—but in fact it is impossible to estimate the amount. Nor can one know in advance whether or not such agencies would create troublesome short-term capital movements into and out of the country. All in all I would favour permitting foreign banks to establish agencies in Canada, but because all the repercussions of such a move cannot be known in advance, I would think that any agency licences granted should be for a ten-year period—as is the case with bank charters. Furthermore, it should be clearly understood by banks receiving agency licences that the experience of the first ten years might require basic modifications in the agency system in the next revision of the Bank Act. The "rules of the game" should be understood in advance.

#### 7. *Prohibition of loans against bank stocks*

Sec. 75, subsec. 2(2) continues the prohibition against making loans on the security of bank stocks that was introduced in special legislation of 1879. The



conditions that led to it no longer exist and so there is no further need for retaining the restriction. As to what those conditions were at the time, I quote from the *Monetary Times* of Jan. 31, 1879:

...After 1874, a gradual wave of depression set in...One consequence of this has been that it has been found impossible to take up the masses of loans on (new) bank stocks, and they have accordingly been kept floating about, now in one form, and now in another, held by this broker and that, advanced upon, changing hands from this bank to that bank, month after month, and year after year, until at present there is somewhere about four millions of bank capital (at par value) in this state of suspension. It is upon this amount of floating capital that the prodigious man of speculation has been built up, which is one of the greatest evils of the time. Operators know that this immense field lies open to them, in which to form their combinations and carry out their plans either for a rise or fall. Bank stocks, therefore, have been for years buffeted about, and tossed up and down at the mercy of speculators.

Since present day conditions do not even remotely resemble those of 1879, I would recommend that the prohibition be limited to loans against a bank's own stock.

## APPENDIX "Z"

Submission to the  
Standing Committee of the House of Commons on Finance, Trade and Economic  
Affairs  
on  
Bill C-222, an Act respecting Banks and Banking  
by  
(PROFESSOR JACOB S. ZIEGEL)

October 29, 1966.

1. My name is Jacob S. Ziegel, and I am a professor of law at McGill University. I specialize in the area of commercial law and, while I lay no claim to being a banking expert, I am interested in several aspects of Bill C-222. It is only these aspects that I feel qualified to discuss in these submissions, and my silence on the other provisions of the new Bill should not be construed as amounting to support or opposition to them. Because of the pressure of other commitments I have had to keep my observations short, but if the Committee would wish me to enlarge on any of them—in person or in writing—I should be happy to do so.

*I Elimination of the Interest Ceiling.*

2. Subject to one reservation (see *infra*, SS8-9), I support the Government's proposals to remove the existing restrictions on the maximum rate of interest which the chartered banks may charge for loans. It follows that I also support the recommendations of the Royal Commission on Banking and Finance dealing with the same subject. I am not qualified to discuss the purely economic merits of these proposals, but I should like to offer a number of observations of a legal and general character which seem to me to strongly favour the removal of the existing restrictions.

3. It is generally assumed that section 91 of the present Bank Act effectively limits the banks to a rate of return of 6 per cent on loans and advances made by them. This is an incorrect assumption. Section 91 provides that,

- (1) Except as provided in subsection (2), no bank shall in respect of any loan or advance payable in Canada stipulate for, charge, take, reserve or exact any rate of interest or any rate of discount exceeding six per cent per annum and no higher rate of interest or rate of discount is recoverable by the bank.

The Act does not define the vital word "interest" (or the meaning of "rate of discount"), and the most recent judicial interpretation—that of the Supreme Court of Canada in *A.G. Ontario v. Barfried Enterprises Ltd.* (1964) 42 D.L.R. (2d) 137, [1963] S.C.R. 570—places a very narrow meaning on it, although, admittedly, in a different context. There is no reason to believe, however, that a

court would construe the term more generously for the purposes of the Bank Act. While the court offered no clear definition itself it emphasized that "The day-to-day accrual of interest" is "an essential characteristic", and it held that a "bonus" charge is not "interest"—at least for the purposes of the Interest Act, R.S.C. 1952, c.156. If the decision is applicable in the banking sphere, its practical result would appear to be that the banks are free to increase their effective rate of return on loans by imposing additional charges of one kind or another which eschew the use of the term "interest".

4. This is in fact what the banks have been doing with the acquiescence of the Department of Finance since at least 1955, and as is well known the effective rate of return on the so called "consumer" or "personal loan" schemes operated by them is closer to 12 than 6 per cent per annum. More recently, the banks have also required some of their commercial borrowers to maintain "compensating balances" in their current accounts, and this is another way to circumvent the restrictions in section 91. In this connection, it should be noted that section 93(2) permits banks to levy charges for the keeping of accounts without in any way imposing any ceilings. I should emphasize that I am not criticizing the banks for these practices; my sole purpose is to point out that section 91 can be easily circumvented and in practice is.

5. The problem of defining the meaning of interest in federal statutes is not a new one. It was extensively discussed (*inter alia*) before the Senate Banking and Finance Committee in 1938 in the course of its hearings on the Small Loans Act, and it was in order to avoid the difficulties inherent in the use of the term "interest" that the Act substituted the expression "cost of loan" See s. 2(a) of the Act.

6. The present method of regulating the rate of interest on loans made by banks defies logical analysis. The cost of any loan depends on such factors as (a) the cost of the borrowed funds to the lender; (b) his administrative overheads and the cost of servicing the loan; (c) the element of risk; and (d) the desired net return to the lender. Items (b), (c) and (d) are variable elements and differ with the size of the loan, the character of the borrower, and the type of security offered to the lender. It therefore follows that if interest rates are to be continued to be regulated in the future the Act must either set different ceilings for different sizes of loans and different types of borrowers or set the ceiling at a sufficiently high level to allow full play for the different factors enumerated above. The permissible "cost of loan" under the Small Loans Act, for example, is directly geared to, and varies with the size of the loan.

7. The vice of the 6 per cent ceiling in section 91 is that it allows the banks very little room to manoeuvre. As result the banks must either circumvent the section or deprive large segments of the community of access to bank funds. As often as not the latter may happen. We thus have the cruel paradox to which the Porter Report drew attention (p. 129) that a section which was designed to protect the small borrower in fact militates against his best interests and forces him to borrow funds elsewhere at interest rates which are often well in excess of the rates which banks would charge if they were free to do so. In this connection I would draw the Committees' attention to the results of official inquiries held in recent years in Nova Scotia, Ontario, and Manitoba with respect to lending practices in the second mortgage field. These show that borrowers have been paying private money-lenders up to 50 per cent for loans between \$1500 and



\$5000. Simply to prohibit such abuses is not enough; they can only be effectively eliminated by creating alternative and cheaper sources of funds.

8. The one reservation I have concerning the removal of any interest ceiling is in the area of consumer loans. The Small Loans Act regulates the rates which may be charged by consumer loan companies (excluding banks) and the removal of all restrictions in the case of consumer loans granted by banks might appear to be discriminatory. I believe the discrimination, if such it is, could be justified in view of the inherent differences between a chartered bank and a consumer loan company, and moreover there is always the danger that a statutory ceiling may all too quickly become the minimum rate. This is what has happened in the small loans field.

9. When these competing arguments are weighed there may still be a slight balance in favour of imposing a rate ceiling with respect to consumer loans. If this should also be the Committee's opinion, I would suggest that the ceiling be set at 12 per cent per annum on the ceiling balance of the loan. Experience in Canada and the United States shows that such a ceiling would be high enough to permit the banks to offer a full range of consumer loans to the average responsible wage earner. An attempt to impose a graduated scale along the lines existing in the Small Loans Act should, I think, be rejected as unnecessarily complicated. The Bill would of course have to include a definition of "interest" or "cost of loan".

#### *II Disclosure of the True Cost of Bank Loans.*

10. For many years now various consumer groups, legislators like Senator Croll, and University scholars in the various disciplines have urged that finance charges in all types of consumer credit agreements should be required to be stated in terms of an effective annual percentage rate as well as in Dollars and cents. The proposal again won very strong support at a Conference on Consumer Credit held at the University of Saskatchewan on May 2-3, 1966, whose proceedings have now been published.

11. Bill C-222 contains no such requirements. The Minister of Finance announced however at the beginning of October that the Government intended to introduce such provisions after all—presumably at the Committee stage of the Bill—and I, for one, warmly welcome the announcement. Federal initiative in this sphere is most important since the Provinces have shown themselves to be reluctant to promulgate similar legislation at the Provincial level unless and until financial agencies subject to federal control are also made subject to disclosure requirements.

12. While I have not seen the amendments which the Minister of Finance proposes to move to the Bill, my impression is that the disclosure requirements will only apply to the information contained in the loan agreement signed by the borrower. In my opinion the amendments should go beyond this stage and also require the same information to appear in any advertisements distributed by the banks. With respect to this question, I would respectfully refer the Committee to a passage in the evidence which I gave before the Special Joint Committee of the House of Commons and Senate on Consumer Credit on November 10, 1964, in which I submitted that (Proceedings of the Special Joint Committee, No. 10, Appendix L, p. 478):

“(d) The advertising practices of the banks should be regulated to the extent of requiring their advertisements to disclose information similar to

that now required in the United Kingdom from hire-purchase companies under the Advertisements (Hire-Purchase) Act, 1957. That is to say, banks which purport to advertise details of their loan schemes should be required to disclose the actual cost of the loan, stated in the same way as they would be required to do in the agreement itself. The banks do not appear to follow this practice in their existing advertisements."

13. Another desirable amendment would be one requiring banks to provide borrowers with a copy of any agreement signed by them. Whether all the banks do it now as a matter of good practice I cannot say, but in any event I think it desirable to put the requirement on a statutory footing. An increasing number of Provincial Acts dealing with consumer credit now impose such a requirement on provincial financing agencies and it is desirable to avoid any suggestion of discrimination in favour of the banks.

### III. *Disclosure Requirements in Personal Savings Accounts.*

14. In my opinion the information supplied to depositors in the pass books issued to them with respect to such accounts is seriously deficient in one important respect. It does not tell the depositor how often and on what basis he is credited with interest earned by his account. As I understand it, the practice is for the banks to compute the interest every three months on the *lowest* amount standing to the credit of the account during the affected period. Thus if \$500 is deposited, say, on the first day of the accounting period and is withdrawn one day before the end of the three months the depositor would receive no interest with respect to that deposit because it had not stayed in his account for the full period. I am not saying this is an unconscionable practice; there may be sound practical reasons for handling savings accounts in this way. What I do say is that many depositors are not aware that this is the basis on which interest is computed. No doubt they could ascertain the facts if they made inquiries, but in my submission the information should be given to them automatically as soon as they open the account.

15. The banks are also uncommonly discreet in advertising the *rates* of interest paid on personal savings accounts. The information is not contained in the pass book and it is not prominently displayed in the precincts of the banks. The rates are varied from time to time (though not very often) and I realize this factor makes it impracticable to insert the information in the pass book. But I see no reason why the information could not be readily communicated to the depositor by other means. He should not have to enquire about it.

### IV. *Wider Representation on the Boards of Directors of Banks.*

16. In 1962, 28.8 per cent of all bank loans were made to private borrowers. This compares with the figure of 52.4 per cent for loans to businesses, (Porter Report, Table 7-3, p. 123). Loans to individuals rank in importance second only to businesses. Nevertheless, as a glance will show at the list of directors of any bank, consumers are conspicuous only by their lack of representation on the boards. This is a regrettable state of affairs and one which ought to be remedied. Even from a narrow profit motive the presence of "consumer representatives" could be easily justified; but beyond that banks are in essence semi-public institutions with important privileges and this status should be reflected in more representative boards. Section 22 of the present Act prescribes that directors are



to be elected, I urge that the section be amended so as to empower the Minister of Finance to appoint additional directors (perhaps of a special character and with limited voting powers) where he is of the opinion that a particular Board is not sufficiently representative of the major interests served by the banks.

*V. The Security Provisions in Bill C-222.*

17. For many years the traditional view was that banks should only lend against the security of collateral which was of a highly liquid and easily realizable character. This philosophy still finds expression in section 75(2)(d) of the Bank Act. Over the years, however, the national interest and business expediency dictated relaxation of the original restrictions and this development is reflected in sections 82-88 of the Act. The Porter Commission recommended that the banks should now be allowed to determine their own forms of security, and the government has accepted this recommendation in section 75(1)(c) of the Bill. This provides, *inter alia*, that a bank may "(c) subject to subsection (3), lend money and make advances upon the security of, and take as security for any loan or advance made by any bank or any debt or liability to the bank, any real or personal, immovable or moveable property...". For a variety of reasons I welcome and support this amendment.

18. In view of this basic change in policy one would have expected the draftsmen to review the other provisions in the Act (principally those in sections 82-90) and either to delete those which are now redundant or at least to modify them in the light of the new policy. Moreover, past experience has shown that there are some serious ambiguities, omissions, and injustices in the existing provisions. The fact remains however that most of the existing provisions have been copied verbatim in the Bill. To deal adequately with the objections to this procedure would require a separate paper. I shall therefore content myself with a list of some of the more important objections:

- (1) There is a conflict between section 75(1)(c)-(d) and sections 82, 85, 86 and 88 of the Bill. S.75(1)(c)-(d) empowers a bank to lend to any person and on any security; the latter sections empower a bank to lend to certain types of persons and against particular types of security. They are therefore either redundant or they may be construed as restricting the general provisions in s. 75(1). Presumably this was not the draftsman's intention.
- (2) Section 75(1)(c) is dangerously vague on such important questions as (a) may a bank take security on future or after-acquired property? (b) may it take security for past indebtedness? (c) is the validity and order of priorities of such security to be governed by Provincial law and, if so, which law?
- (3) No attempt has been made to correct such omissions, ambiguities and injustices in sections 82, 86, and 88 as the following: (a) does a bank have a first lien on the proceeds of sale of a section 88 security? (b) does the rule in *Hopkinson v. Rolt* (1861) 9 H.L.C. 514 apply to a s. 88 security? (c) can the bank's lien under ss. 86 and 88 be cut off or subordinated by the sale of the goods to a bona purchaser in ordinary course of business or to a person who acquires a common or civil law lien or privilege in respect of services provided by him? Particularly distressing is the retention of the provisions in ss. 82(4) and 89(1) to



the effect that a bank's lien under these sections is not subordinated to the lien of an unpaid vendor unless the bank has knowledge of the lien. These provisions have provoked considerable litigation and are unjust to conditional sellers and to vendors with a right of resiliation under Quebec law. (Even registration of the lien would not help the vendors since ss. 82, 89 require actual knowledge on the part of the bank).

- (4) There is no consistency in the provision in dealing with such basic questions as the creation of the security interest, its perfection, priorities between conflicting claims, and methods of enforcing the security. For further particulars see Ziegel & Feltham, "Federal Law and a Uniform Act on Security in Personal Property" *Canadian Bar Journal*, February 1966, p. 30, esp. at p.33. (An offprint of the article is attached to these submissions).
- (5) No attempt is made to integrate the federal provisions with the corresponding Provincial provisions. This needlessly complicates everyday commercial transactions throughout the country.
- (6) Sections 75-90 are not arranged in logical order: e.g., ss. 83-84 (which deal with liens on bank shares and the right of a bank to own immoveable property) are sandwiched between two sections dealing with loans made against the security of hydrocarbons and the making of loans to receivers and liquidators.

Considerations such as the above lead irresistibly to the conclusion that the security provisions in the new Bill should be completely reviewed and rationalized in the light of the best modern thinking on the subject. This process has recently been completed in the United States in Article 9 of the Uniform Commercial Code and is presently receiving attention in several of the Canadian Provinces. I would particularly draw the Committee's attention to the Draft Ontario Personal Property Security Act Bill which is likely to be enacted in the near future and to the efforts of a special committee of the Canadian Bar Association to promote a model bill on the same subject.

#### Appendix

Offprint from the Canadian Bar Journal

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## Federal Law and a Uniform Act on Security in Personal Property<sup>\*</sup>

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(This paper was originally prepared for the use of the Committee on a Uniform Law on Security in Personal Property of The Canadian Bar Association and is reprinted here with the thought that it may be of interest to a wider audience. It has been brought slightly up to date and other minor changes have been made to it.)

<sup>\*</sup>Reprinted by courtesy of the Canadian Bar Journal.

### *Constitutional Background*

The creation of security interests in personal property would ordinarily be regarded as an aspect of the regulation of property and civil rights and therefore as falling within the provincial jurisdiction by virtue of section 92(13) of the British North America Act. Nor does section 91 alter this position by expressly assigning this field to the legislative competence of the federal government. However, the regulation of security interests may legitimately be regarded as incidental to many of the heads of jurisdiction which are assigned to the federal government in the BNA Act, and it is no doubt on this basis that Parliament has proceeded in adopting provisions dealing with security in personal property in more than a dozen Acts.

In the leading case, *Tennant v. Union Bank of Canada* [1894] A.C. 31 the appellant argued that the provisions of the Bank Act (46 Victoria, c. 120, ss. 53 and 54) dealing with warehouse receipts as security were *ultra vires* the Parliament of Canada. The Board (per Lord Watson) decided that "banking" is "an expression which is wide enough to embrace every transaction coming within the legitimate business of a banker." (page 46). Lord Watson went on to say:

"The appellant's counsel hardly ventured to dispute that the lending of money on the security of goods, or of documents representing the property of goods, was a proper banking transaction. Their chief contention was that, whilst the Legislature of Canada had power to deprive its own creature, the bank, of privileges enjoyed by other lenders under the Provincial law, it had no power to confer upon the bank any privilege as a lender which the Provincial law does not recognize. It might enact that a security, valid in the case of another lender, should be invalid in the hands of the bank, but could not enact that a security should be available to the bank which would not have been effectual in the hands of another lender. It is said, in support of the argument, that the first of these things did and the second did not constitute an interference with property and civil rights in the province. It is not easy to follow the distinction thus suggested. There must be two parties to a transaction of loan; and if a security, valid according to Provincial law, was made invalid in the hands of the lender by a Dominion statute, the civil rights of the borrower would be affected, because he could not avail himself of his property in his dealings with a bank."

"But the argument, even if well founded, can afford no test of the legislative powers of the Parliament of Canada. These depend upon sect. 91, and the power to legislate conferred by that clause may be fully exercised, although with the effect of modifying civil rights in the Province; and it appears to their Lordships that the plenary authority given to the Parliament of Canada by sect. 91, sub-sect. 15, to legislate in relation to banking transactions is sufficient to sustain the provisions of the Bank Act which the appellant impugns." (page 46).

It follows that the test is whether the provisions relating to security are properly ancillary to the subject assigned to the Parliament of Canada. The decision in the *Tennant* case appears to lean towards generosity in defining the

extent of the federal power in this regard. See also *Royal Bank of Canada v. Larue* [1928] A.C. 187; and Falconbridge, *BANKING AND BILLS OF EXCHANGE*, 6th ed., 1956, pp. 22 ff.

### *Federal Laws*

Broadly speaking, the federal provisions fall into one or more of the following categories:

I. Those which authorize the taking of security but, by implication, leave the determination of its form and all other matters to provincial law: see

Farm Credit Act, Stat. Can. 1959, c. 43 as am., s. 11(1)

Bank Act, 1953-4, c. 48, ss. 75(6), 78(1) & (2), 83, 85(1).

Industrial Development Bank Act, R.S.C. c. 151 as am., ss. 16, 23.

Small Businesses Loans Act, 1960-1, c. 5 as am., s. 8.

II. Those which establish their own schemes for the perfection of security interests but, by implication, leave all other questions to be decided by provincial law (or, *quære*, federal common law): see

Railway Act, R.S.C. c. 234, ss. 134-148.

Canada Shipping Act, R.S.C. c. 29 as am., ss. 45 et seq.

Copyright Act, R.S.C. c. 55, s. 40.

Patent Act, R.S.C. c. 203 as am., ss. 52-3.

Trade Marks Act, 1952-3, c. 49, ss. 26(1), 64(c), & S.O.R. 1955 Cons., Vol. 3, p. 2849, s. 58.

III. Those which regulate the creation of a security interest and all other aspects of the secured transaction but require compliance with provincial laws with respect to matters of perfection: see

Bank Act, *supra*, 82(5) and s. 89(2).

IV. Those which purport to regulate all aspects of the secured transaction: see

Bank Act, *supra*, ss. 86, 88 et seq.

Farm Improvement Loans Act, R.S.C. c. 110 as am., s. 6, & S.O.R. 1955 Cons., Vol. 2, P. 1269.

Industrial Development Bank Act *supra*, s. 19.

V. Those which avoid the security interest in bankruptcy unless it has been perfected in accordance with provincial registration requirements: see

Bankruptcy Act, R.S.C., c. 14, s. 63.

Section 64 of the Bankruptcy Act dealing with preferences and other provisions of that Act dealing with secured interests should also be noted in this connection. It is established that the Bankruptcy Act is paramount to provincial legislation: *Royal Bank of Canada v. Larue*, *supra*.

VI. Miscellaneous provisions: see

- (a) Municipal Development & Loan Act, 1963, c. 13, s. 21 & S.O.R. 1963, p. 1132, s. 6. This establishes a procedure for the sale of municipal securities held as security.



- (b) Companies Act, R.S.C. c. 53 as am. 1964-5, c. 52, s. 66. This establishes requirements for the filing of certain types of mortgages and charges created by federal companies.
- (c) Quebec Savings Banks Act, R.S.C. 1952, c. 232, ss. 34-41. This authorizes certain types of security and regulates to some extent the method of realizing on it (ss. 38-40) and the effect of disposal of security by a bank (s. 41).
- (d) Canadian Fisherman's Loan Act, R.S.C. 1952, c. 37, s. 7. This purports to give priority to the Crown's security over all other liens and charges.
- (e) Canada Shipping Act, R.S.C. 1952, c. 29, ss. 5, 45-62. These provisions regulate the sale and transfer of interests in vessels and the perfection and priorities of mortgages granted with respect to them.

From the above list it will be seen that the federal provisions are almost as numerous and diverse in character as are the provincial provisions. Moreover, as in the case of the Bank Act, the same federal Act may deal with security interests in a variety of ways. Thus, if a bank takes a chattel mortgage from a consumer under section 75(6) of the Bank Act, the transaction will be governed wholly by provincial law; if it takes a security interest in hydro-carbons under section 82, it will be governed partly by federal and partly by provincial law; and if it takes a section 88 security, all aspects of the transaction (save in one instance: see s. 89(2)) will be governed by federal law.

To complete the picture, it must be noted that the federal provisions are frequently incomplete, ambiguous or otherwise unsatisfactory. This is particularly true of some of the provisions of the Bank Act. To illustrate:

1. The Companies Act (s. 66) requires particulars of mortgages and charges created by federal companies to be filed with the Secretary of State, but imposes only a fine for non-compliance (s. 66(9)). On the other hand, the Act appears to make no provisions for late filing.
2. The Copyright Act (ss. 40, 40(3)) and the Patent Act (ss. 52-3) require respectively the registration of every assignment of a patent or any grant of an interest in a copyright. "Assignment" and "interest", however, are not defined, and it is not clear whether they include an assignment by way of security or the grant of a security interest. The regulations made under the Trade Marks Act contain a similar requirement, but fail to state what is the sanction in the case of non-compliance.
3. Section 86 of the Bank Act empowers a bank to take as security a bill of lading or a warehouse receipt and provides that in such an event the Bank shall be vested with all the rights in the goods possessed by the pledgor. The definitions of "bill of lading" and "warehouse receipt" in section 2 of the Act do not distinguish between negotiable and non-negotiable documents of title or between a document of title and a mere receipt for goods, with the result that a bank which takes a section 86 security appears to obtain a good title to the goods by mere delivery of the document, even though it is non-negotiable and the bailee has not been notified of the transfer

and has not attorned to the bank. This involves a marked departure from the common law rules and the provisions of the Uniform Warehouse Receipts Act and may easily create a conflict with the provincial law under which the original document was issued. (Cf. Baxter, *THE LAW OF BANKING*, pp. 216-7).

4. Section 88 of the Bank Act is defective in many respects. It fails to state, for example, whether or not the bank has a security interest in the proceeds of the sale of any goods held as security—a question of great practical importance. (See, e.g. *Flintoft v. Royal Bank of Canada* [1964] S.C.R. 631 (S.C.C.) and cf. *LeDain*, 2 McGill L. J. 77 at pp. 103-111 and Ziegel, 41 Can. Bar Rev. 54 at pp. 66-9). Nor does s. 88(5), the priority section, make it clear whether or not the rule in *Hopkinson v. Rolt* (1861) 9 H.L.C. 514 applies or to what extent a purchaser of the goods from the debtor takes free of the bank's security interest.

Regardless, therefore, of whether or not the federal provisions are integrated with the provincial laws, there is a strong case for revising and improving them.

The principal question remains, however; and this is whether there is a continued need for the federal provisions at all. From what we have already described, it will be obvious that their existence—differing as the provisions do in many respects from the corresponding provincial laws—greatly complicates the security picture in Canada. In this respect, the American position appears to be much simpler since, for a variety of reasons, there is much less federal legislation on the subject than there is in Canada. Most importantly, American banks are generally subject to state jurisdiction and even those banks which are incorporated under federal law appear to be subject to no restrictions with respect to the type of security they may take in personal property. See 12 U.S.C.A., ss. 24, 29.

We think the answer to our question falls into two parts. First, there are the federal provisions which, like those in the Copyright, Patent and Trade Marks Acts, establish a system of registration for security interests in the types of collateral regulated by these Acts, but leave all other questions to be decided by provincial law. These provisions are needed and should be retained. The Acts deal, in part at least, with questions of ownership and require the federal authorities to maintain records of ownership. It seems convenient, therefore, that security interests in such collateral should also be recorded in the same register. The same approach is adopted in the Uniform Commercial Code. U.C.C. 9-302 (3)(a) provides that the filing provisions of Article 9 do not apply to a security interest in property subject to a statute of the United States which provides for a national registration or filing of all security interests in such property.

Secondly, there are those very important federal provisions which, like those in sections 82, 86 and 88-90 of the Bank Act, purport to regulate all aspects of a given secured transaction. These provisions have a long history and were first introduced with the laudable object of encouraging the chartered banks to provide short-term loans to primary producers, distributors and manufacturers and to enable the banks to obtain a security in simple form. Having regard to the state of the common and statutory law which obtained in the last century (and,



for that matter, still obtains) these objectives could not have been attained under provincial law. There was a need, therefore, for the federal provisions.

The position is now radically changed in the draft Ontario Personal Property Security Act and would, it is safe to assume, be changed in any uniform act based on the Ontario Bill. Subject to one reservation to which we shall refer in a moment, inventory financing will in future be as simple and safe under any enactment based on the Ontario draft Act as it is under the Bank Act. With one exception, the latest revision of the draft Act abolishes the need for all affidavits (cf. ss. 10(b), 15, and 48(1)); it permits the taking of a *legal* security on present and after-acquired property to secure present and future advances (s. 13); and, generally, it permits any agreements to be given effect according to its tenor (s. 9).

The Bill also offers advantages not found in the Bank Act. First, its provisions are much more carefully drawn and much more detailed than those in the Bank Act. Secondly, the Bill confers on the inventory financier a continuously perfected security in the proceeds of any sale (s. 28), thus resolving a point which has given rise to much litigation in Canada. Thirdly, since all security interests in personal property are governed by the same act and are subject to a single set of basic provisions, the financier can take security in the same agreement in other collateral as well as in the debtor's inventory. If he does so, he will need to register only one document in one place (where the security is non-possessory in character), and will, if the necessity arises, have to observe only one set of rules if he wishes to enforce any part of his security. From all of this it follows that if, at some future date, the security which the banks may take under sections 82, 86 and 88 of the Bank Act were to be made subject to provincial law, the banks would be no worse off; in many respects they would be better off. What we have said with respect to the Bank Act applies, *mutatis mutandis*, to the security provisions in the other federal acts. The merger of the federal and provincial security laws would not, of course, affect those federal provisions which prescribe what *kinds* of collateral banks and other institutions subject to federal control may accept as security.

We have one reservation concerning the suitability of the Ontario draft Act for inventory financing, and this involves its filing requirements. Section 48 of the draft Act requires the original security agreement or a counterpart thereof to be filed, and the agreement must contain, *inter alia*, a description of the collateral "sufficient to identify it". Section 88(4) of the Bank Act, by contrast, requires only a Notice of Intention to give a section 88 security to be filed, and this Notice does not even have to describe the collateral. See Schedule K to the Act. Having regard to the special features of inventory financing, we believe the notice filing approach is the correct one. It is also adopted in U.C.C. 9-401. This matter received considerable attention at the Osgoode Hall Conference held in May, 1964, and many participants favoured the notice filing concept. We recommend, therefore, that any uniform act which may eventually be adopted will also incorporate this feature.

Finally, it remains for us to consider what are the prospects of the federal government repealing its security provisions and allowing a uniform act to govern (subject to the exception we have suggested as being appropriate) all aspects of any security interest, including those created by or in favour of any person subject to federal jurisdiction. In our opinion, the adoption by the



federal government of its own security act would not be a satisfactory alternative since it would not eliminate the problem of having two concurrent jurisdictions over the same collateral.

We have not discussed the question with any federal officials and the views we are about to express are our own and speculative in character. It seems reasonable to expect, however, that the federal government will be largely guided by the views of the chartered banks, they being the bodies most closely concerned with any change in the federal law. It further seems reasonable to assume that the banks will not support such changes unless they are satisfied (a) that the changes will not affect their interests adversely; (b) that they are in the interests of the business community; (c) that there is a reasonable prospect of the uniform act being widely adopted across Canada; and (d) that the uniform act will not be amended unilaterally by any province which has adopted it. The first and second conditions can be met by ensuring that the banks and other important sections of the business community are consulted continuously throughout the drafting of the uniform act. The third and fourth conditions are likely to create greater difficulties. It seems indeed unlikely that the federal government will seriously consider any legislative action until it has seen how much provincial support the uniform act has received. This possibility merely emphasizes the importance of the provincial and federal governments being closely associated with the work of the national Committee through the Conference of Commissioners on Uniformity of Legislation in Canada and otherwise. Given a seriousness of purpose, however, and the active support of the Bar, we see no reason why a single security law applicable at both levels of government could not become a reality in the foreseeable future.

### Appendix

Reprinted below are the Sections in the revised Draft Ontario Personal Property Security Act to which reference is made in the memorandum. The full text of the draft Act appears in an appendix to Report No. 3 of the Ontario Law Reform Commission on Personal Property Security Legislation, dated May 28, 1965. For the history of the draft Act and discussions of it, see Ziegel, (1963) 6 Can. Bar Jl. 374 and symposia in (1964) 7 Can. Bar Jl. 278 and (1965) 30 Sask. Bar Rev. 203.

*Section 9.* Except as otherwise provided by this or any other Act, a security agreement is effective according to its terms between the parties to it and against third parties.

*Section 10.* A security interest is not enforceable by or contains a description unless,...

- (b) the debtor has signed a security agreement that contains a description of the collateral and, if the collateral is or includes fixtures or crops, or oil, gas or other minerals to be extracted, or timber to be cut, a description of the land concerned.

*Section 13.* (1) Except as provided in subsection 2, a security agreement may cover the young of animals after conception and after acquired property.

- (2) No security interest shall attach under an after-acquired property clause,

- (a) to crops that become such more than one year after the security agreement has been executed, except that a security interest in crops that is given in conjunction with a lease, purchase or mortgage of land may, if so agreed, attach to crops to be grown on the land concerned during the term of such lease, purchase or mortgage; or
- (b) to consumer goods, other than accessions, unless the debtor acquires rights in them within ten days after the secured party gives value.

*Section 15.* Where a security agreement creates or provides for a purchase-money security interest in other than consumer goods and includes collateral in addition thereto, it shall be accompanied by an affidavit of the debtor (Form 2) stating,

- (a) that the debtor is fully aware of the nature of the transaction and that he knows that the security interests extends to personal property in addition to that included in the purchase-money security interest; and
- (b) that the security interest was not created in fraud creditors.

*Note:*—This section did not appear in the original draft Act and was added by the Law Reform Commission. It has been the subject of some criticism. No sanction is *semble* provided of non-compliance with its provisions.

*Section 48.*—(1) In order to register under this Act for the purpose of perfecting a security interest, the security agreement or a copy thereof signed by the debtor shall, subject to Subsection 2, be registered, and it shall contain and legibly set forth at least,

- (a) the full name and address of the debtor;
- (b) the full name and address of the secured party;
- (c) the date of execution of the security agreement;
- (d) a description of the collateral sufficient to identify it;
- (e) the terms and conditions of the security agreement; and
- (f) where appropriate, the affidavit provided for in section 16. (*sic*).







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LÉON-J. RAYMOND,  
*The Clerk of the House.*

HOUSE OF COMMONS

First Session—Twenty-Seventh Parliament

1966-67

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STANDING COMMITTEE

ON

FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. HERB GRAY

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MINUTES OF PROCEEDINGS AND EVIDENCE

No. 34

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TUESDAY, JANUARY 10, 1967

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Respecting

Bill C-190, An Act to amend the Bank of Canada Act.

Bill C-222, An Act respecting Banks and Banking.

Bill C-223, An Act respecting Savings Banks in the Province of Quebec.

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WITNESSES:

Messrs. Joseph Pope; R. G. D. Lafferty; and Terry Howes.

ROGER DUHAMEL, F.R.S.C.  
QUEEN'S PRINTER AND CONTROLLER OF STATIONERY  
OTTAWA, 1967



STANDING COMMITTEE  
ON  
FINANCE, TRADE AND ECONOMIC AFFAIRS

*Chairman:* Mr. Herb Gray

*Vice-Chairman:* Mr. Ovide Laflamme

and Messrs.

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Basford,  
Cameron (*Nanaimo-  
Cowichan-The Islands*),  
Cashin,  
Chrétien,  
Clermont,  
Coates,

Comtois,  
Flemming,  
Fulton,  
Gilbert,  
Irvine,  
Lambert,  
Lamontagne,  
Latulippe,

Leboe,  
Lind,  
McLean (*Charlotte*),  
Monteith,  
More (*Regina City*),  
Munro,  
Valade,  
Wahn—(25).

Dorothy F. Ballantine,  
*Clerk of the Committee.*

## MINUTES OF PROCEEDINGS

TUESDAY, January 10, 1967.

(68)

The Standing Committee on Finance, Trade and Economic Affairs met at 11:05 a.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Cameron (*Nanaimo-Cowichan-The Islands*), Clermont, Comtois, Flemming, Gilbert, Gray, Laflamme, Lambert, Lind, McLean (*Charlotte*), More (*Regina City*)—(11)

*In attendance:* Mr. Joseph Pope, Pope and Company, Toronto; Mr. Denis Baribeau and Miss M. R. Prentis, research assistants.

The Chairman presented the Eighth Report of the Sub-Committee on Agenda and Procedure dated December 21, 1966, which is as follows:

Your Sub-Committee on Agenda and Procedure met at 1:00 p.m. this day and has agreed to recommend as follows:

- (a) That the undermentioned be invited to present their briefs to the Committee on the dates shown:

*January 10*—R. G. D. Lafferty, Montreal; Joseph Pope, Toronto; Terry Howes, Erindale, Ont.

*January 12*—Frank O'Hearn, Scarborough; Melvin A. Rowat, Elmvale, Ont.; Harry H. Hallatt, Scarborough.

*January 17*—Canadian Federation of Agriculture CUNA International Inc.

*January 19*—Mercantile Bank of Canada

- (b) That your Sub-Committee consider at a later date the timing of the hearing for Bill S-25, An Act to incorporate The North West Life Assurance Company of Canada, which has been referred to the Committee.

The Chairman reported that it has since been learned that the Mercantile Bank of Canada will be unable to appear on January 19th, but they have agreed to appear on January 24th, and he therefore suggested that a motion to approve the report of the Sub-Committee should include the appropriate amendment regarding the date of appearance of the Mercantile Bank.

On motion of Mr. Clermont, seconded by Mr. Lambert, the Report of the Sub-Committee on Agenda and Procedure was approved, as amended.

The Committee resumed consideration of the banking legislation.

The Chairman introduced the witness, Mr. Pope, who read his brief and was questioned. In accordance with the resolution passed at the meeting of October 13, 1966, Mr. Pope's brief is attached as *Appendix CC*.

The questioning having been concluded, the Chairman thanked the witness who was permitted to retire.

At 1:00 p.m. the Committee adjourned until 3:45 p.m. this day.

#### AFTERNOON SITTING

(69)

The Committee resumed at 3:50 p.m. this day, the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Addison, Cameron (*Nanaimo-Cowichan-The Islands*), Clermont, Comtois, Flemming, Gilbert, Gray, Laflamme, Lambert, Lind, McLean (*Charlotte*), More (*Regina City*)—(12)

*In attendance:* Mr. R. G. D. Lafferty, Lafferty, Harwood and Company, Montreal; Mr. Baribeau and Miss Prentis.

The Chairman introduced the witness, Mr. Lafferty, who summarized his brief and was questioned. In accordance with the resolution passed at the meeting of October 13, 1966, the brief is attached as *Appendix DD*.

The questioning continuing, at 5:50 p.m. the Committee adjourned until 8:00 p.m. this day.

#### EVENING SITTING

(70)

The Committee resumed at 8:10 p.m., the Chairman, Mr. Gray, presiding.

*Members present:* Messrs. Cameron (*Nanaimo-Cowichan-The Islands*), Clermont, Comtois, Fulton, Gilbert, Gray, Laflamme, Lambert, Lind, McLean (*Charlotte*), More (*Regina City*), Wahn—(12)

*In attendance:* The same as at the afternoon sitting and Mr. Terry Howes, Erindale, Ontario.

Questioning of Mr. Lafferty was continued and concluded. The Chairman thanked the witness who was then permitted to retire.

Mr. Howes was called and questioned. In accordance with the resolution passed at the meeting of October 13, 1966, Mr. Howes' brief is attached as *Appendix EE*.

The questioning having been concluded, the Chairman thanked the witness who was permitted to retire.

At 10:35 p.m. the Committee adjourned until Thursday, January 12, 1967.

Dorothy F. Ballantine,  
*Clerk of the Committee.*



## EVIDENCE

(Recorded by Electronic Apparatus)

TUESDAY, January 10, 1967.

The CHAIRMAN: Gentlemen, we are now in a position to begin our meeting. It will be basically for the purpose of taking evidence. Our witness this morning is Mr. Joseph Pope, proprietor of Pope and Company, which is a member of the Montreal Stock Exchange, the Investment Dealers Association of Canada, and I gather also an associate member of the Boston Stock Exchange and the Philadelphia-Baltimore-Washington Stock Exchanges. Prior to forming his own firm, Mr. Pope spent a number of years with one of the chartered banks and with a major investment firm. Since Mr. Pope's brief is actually brief, rather than attempt to have him summarize it, I am going to ask him to read it to us and then we will enter into our discussion.

Mr. JOSEPH POPE (*Pope & Company, Toronto*): Mr. Chairman and hon. gentlemen. A section of the Bank Act that has received little or no public discussion and yet is far reaching in its effect is section 157. I refer to the new draft. This section was first introduced in the revision that took place in the 1930s. On the face of it, the section would appear to have been inserted merely to forbid an improper use of the word "bank" by unsound institutions wishing to take advantage of the gullibility of the public. In practice, it has brought about greater evils in that by forbidding the use of the words "bank", "banker", or "banking" by those who are not incorporated under the terms of the Bank Act, it has effectively made it impossible for even those foreign banks of the highest repute to offer their services to the Canadian public.

The point that this memorandum wishes to emphasize is that it is not generally realized that the results of this section 157 have been, unwittingly, quite disastrous.

*Firstly*: By using the word "bank" in this manner, Parliament has in effect changed the normal meaning of the word as commonly used in the English language; as an unfortunate legal implication is that any institution carrying on business in Canada and performing banking functions, but not chartered under the Bank Act, is beyond the control of the federal Parliament. This, of course, is quite contrary to the thought of those who drafted the British North America Act.

*Secondly*: As the international banks are, as a consequence of this section, forbidden to open branches in either Montreal or Toronto, our public suffers from a considerable limitation in the banking facilities that are offered to it. This is not necessarily a criticism of the facilities offered by our own chartered banks. As we all know, these rank amongst the soundest in the world. The point is, though, that while they are excellent in their chosen fields—and by that I refer to normal commercial banking and savings banking—they are somewhat pro-

vincial in their approach to international banking. Parliament should not put itself in the position of depriving the public of the more sophisticated banking services that are available in foreign financial centres.

*Thirdly:* Section 157 actually reduces Canada, in matters of international finance, to the status of a third-rate power. It is no exaggeration to say that, financially speaking, the influence of the Canadian dollar abroad is practically nil.

*Fourthly:* The Canadian dollar, because of this section 157, is merely a local currency rather than an international currency.

*Fifthly:* Properly speaking, there is no foreign exchange market in Montreal or Toronto worthy of the name. One grants that the foreign exchange trading departments of the various chartered banks are quite adept at making quotations in American dollars, yet the fact remains that any quotation in Canadian dollars for any other foreign currency is merely a reflection of the New York market.

*Sixthly:* It is again no exaggeration to say that this section has been responsible over the years for the loss by our exporters and manufacturers of a great deal of business. Manufacturers can well have excellent products for sale, but lacking complete financial advice regarding foreign exchange and foreign credit, they are unable to compete with those who have more financial expertise at their disposal.

It is sheer emotional chauvinism to believe that foreign banks are anxious to come into this country to prey on the savings of our widows and orphans. The finest financial centre in the world is London. In that city there are nearly two hundred branches of foreign banks. Of course about a dozen of them are our own Canadian banks. The requirements for the starting of a branch of a foreign bank in London are quite simple. It is merely required that it be licensed by the London Board of Trade, and on its letterhead state the country and year of its incorporation. Contrary to the fears of our chartered banks, a branch of a foreign bank does not deprive local banks of business, but rather brings new business to the financial community. Mr. Chairman, I would like at this time to suggest that my next paragraph on subsection G be removed because it concerns a matter upon which you have had testimony from far more expert witnesses than myself. So, if you like I will just take out that paragraph.

The CHAIRMAN: Well you are as much entitled to present your views on this topic as any other citizen who has indicated a desire to appear before us.

Mr. POPE: Well, I have made a reservation which you have noted.

The CHAIRMAN: Yes, we have noted it.

Mr. POPE: You have noted it gentlemen. By the same token, sub-section "G" of section 75 of Bill C-222 must be considered iniquitous. It is perfectly proper for Parliament to pass legislation seeing to it that foreign guests behave as good citizens. It is another matter entirely though to propose legislation aimed at causing needless harm to a particular well-behaved foreign guest.

The restrictions imposed on ownership of bank shares by the new section 53 are to be deplored. Sub-section 2 of section 53, which limits the shares of a chartered bank that may be held by one group to 10 per cent merely serves to perpetuate control by management rather than control by the owners, which is the more proper thing.

Much of the newspaper discussion regarding the revision of the Bank Act has been on the matter of whether or not a limit should exist on the rate of interest that chartered banks may ask for in granting loans. Most of the arguments in favour of retention of the rate ceiling tend to be emotional rather than rational. There are no sound grounds for believing that the chartered banks would take advantage of this new freedom, were it granted to them, by charging rates that could be considered improper. At the present time, the limit is quite unrealistic and produces unhealthy results.

All of which is respectfully submitted,

The CHAIRMAN: Thank you, Mr. Pope. Before going on, the committee will have to deal with a procedural matter. We are now officially constituted. I should bring to your attention the report of the steering committee of Wednesday, December 21, as follows: (*See Minutes of Proceedings*)

I should point out to the Committee that our Clerk, Miss Ballantine, after looking into this matter appended this note:

All the above have confirmed that they will appear on the dates mentioned, except the Mercantile Bank of Canada, who will not be able to appear until January 24th.

I would suggest to the committee that we have a formal motion to approve the report with the amendment that the Mercantile Bank will appear on the 24th rather than the 19th. Also, I would suggest hopefully that our Clerk might inquire if the group of junior trust companies might be available on that date. Of course I realise this may be a little too soon, but perhaps we may consider having them on that date if other factors, including the deposit insurance resolution, seem to make it convenient. I just suggest this from the point of view of using our time to the best advantage. Could I have a motion of this kind so that we can proceed properly with any discussion on this report.

(*Translation*)

Mr. CLERMONT: I so move.

Mr. LAMBERT: I second the motion.

(*English*)

The CHAIRMAN: Is there any discussion?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Have we had an answer from the Mercantile Bank on the January 24th date?

The CHAIRMAN: Oh yes. We originally suggested the 19th. However, some of the people we would want to hear from were not available on the 19th; they themselves apparently suggested the 24th, and this fits into our order of business. I would suggest to the Committee that this might therefore be an appropriate time to hear from this group. Is there any further discussion? If not, are all in favour of the report as modified?

Some hon. MEMBERS: Yes.

The CHAIRMAN: Thank you.

Mr. LAMBERT: I have a question arising out of that. Have you been able to ascertain when the Minister of Finance will be available?



The CHAIRMAN: I have not pursued the matter since we adjourned for Christmas.

Mr. LAMBERT: I want to come back to the original charge, that a lot of the consideration that we have been given so far is quite academic. The Government is proposing certain changes and we have had no reasoning by the government. It has been quite impossible and quite improper to try to get anything from Mr. Elderkin in connection with, shall we say, the motivation in respect of a number of these changes, which has made a lot of the discussion with the Canadian Bankers Association and others quite frustrating and sometimes futile. The sooner he gets here and puts his case forward the better.

The CHAIRMAN: As you may recall, the approach the committee generally felt was satisfactory was to hear witnesses who had views to express and then have the minister with us for a lengthy period so that questioning of the minister could proceed in the light of the thoughts brought forward by people outside government circles. Anyway, we appear to be almost done with our witnesses. However, I will pursue that aspect further because I think there is no question that we are getting to the stage when the Minister of Finance could make a very useful contribution to our work, and I think we should in any event have the steering committee meeting early next week to come to some definite decision on that point.

May I suggest to the committee that it appears to me that Mr. Pope's brief falls into four sections: his views on the implications of section 157, up to and including the end of the second paragraph on page 2; then there are his remarks on section 75, although, perhaps in fairness to Mr. Pope if he feels that his own expertise does not extend particularly in that direction, you may not wish to discuss this paragraph with him in detail; then his views on subsection 2 of section 53; and finally his views on the interest rate. I would suggest to the committee that we discuss Mr. Pope's brief with him in that order, following which we should have time to raise any other points on which we feel he may have some contribution to make. The first name I have on my list is Mr. Laflamme, followed by Dr. McLean and then Mr. Cameron.

Mr. LAFLAMME: Mr. Chairman, I would just like to know if Mr. Pope was referring to the proposed article 157 in the proposed bill.

*(Translation)*

Mr. POPE: Yes, it is in Bill C-222, sir. It could be found in all bills since 1933, as you know.

Mr. LAFLAMME: I understand, but I would like to know, from the legal point of view, what can eventually be the effect which would be so disastrous with regard to this proposal? What is so wrong about using the word "bank" without providing a definition of that word?

Mr. POPE: But, sir, that is just what is disastrous.

Mr. LAFLAMME: But since there are no legal consequences, what exactly is the nature of that disaster?

Mr. POPE: I see. I was trying to give some broad explanation of the six points, so to speak. The first is that the inclusion of that clause 157 in the Bill

does provide a near-definition of the word "bank". This means that a bank is any institution incorporated under the Bank Act.

This means that nothing else is banking and this is ridiculous. This means that, according to the British North America Act, all banking activities fall under the control of the federal government. But under this clause 157, you limit your control to chartered banks. Trust companies, all sorts of companies that are actually banks, and accept deposits from the public and withdrawals of deposits and cash cheques on demand, are banks in the true sense of the word, in English and in French, but a judge or a lawyer could say: "These are not banks", referring to this clause 157. So you are removing from your control the greater portion of banking operations in the country and you are denying the British North America Act.

Mr. LAFLAMME: You consider that article 157 as it is drawn up, reduces, restricts the meaning of the word "bank"?

Mr. POPE: It changes the sense of the word. There is a sense to this word, a definition to this word in the dictionary:

Mr. LAFLAMME: There is no definition in the Act, even.

Mr. POPE: The words are tricky. Any person who uses the words "banking, or banking operations" who carries on such operations, but does not have a charter is actually against the law. So this means that anyone who is in business, and doing banking business can say "I am not a banker because I do not come under the Bank Act, I was incorporated under the chartered loan corporations in the country—

(English)

Mr. LAFLAMME: —trust and loans Corporations of Ontario.

(Translation)

Mr. POPE: Therefore I am not in the banking business.

Mr. LAFLAMME: Well what would be your suggestion?

Mr. POPE: My suggestion would be that we would do away with this clause. Do you agree with this. This was put in the law in 1930 at a time when all—

(English)

—investment bankers had their tails between their legs because of the depression and the thing has stuck in there ever since. It has had a very evil effect which people do not realize.

Mr. LAFLAMME: Thank you very much.

Mr. McLEAN (Charlotte): Mr. Pope, would you take 157 right out of the Bank Act?

Mr. POPE: Yes, sir.

Mr. McLEAN (Charlotte): Was that not put in, in the first place, because they were designated as bankers and issued their own currency?

Mr. POPE: If you are asking me the question, sir, that is not my understanding. My understanding, sir, is that the Bank Act has been in existence practically as long as this country has been in existence. It was enacted shortly after 1867 and this clause was only put in about 1930, sir.

Mr. McLEAN (*Charlotte*): Yes, but was it not put in because they were designated and set apart as bankers and as such they issued their own currency.

Mr. POPE: By a coincidence, sir, it was about the time this section first went in that the banks had their note issuing—

Mr. McLEAN (*Charlotte*): How would you tell a banker from anybody else if the banks were issuing their currency and the other people were not issuing any currency? Are you not a banker today because of your relations with the central bank and other things?

Mr. POPE: Perhaps that is the definition of the word “bank”, that legislation has forced on us in this country, but it is my submission that banking could be defined in more simple terms than that. One who accepts deposits or who holds himself open to accept deposits payable on demand and, if you like, offers a chequing facility, is a banker.

Mr. McLEAN (*Charlotte*): Would you not come in conflict with the provinces then? Would the federal government not come in conflict with the provinces?

Mr. POPE: No, sir.

Mr. McLEAN (*Charlotte*): It would not?

Mr. POPE: Not in my opinion, sir. I am not a lawyer but since you have raised the point, sir, I would suggest that if a provincial government chartered what they call the trust companies and now these trust companies receive deposits, fine; it is within the jurisdiction of a provincial government to create incorporations with set purposes, but the federal government has authority over banking and if it finds a provincial creature engaged in banking, it may control it under the B.N.A. Act.

Mr. McLEAN (*Charlotte*): Would it do that down in Quebec?

Mr. POPE: Absolutely.

Mr. McLEAN (*Charlotte*): You come, thirdly, to the section which actually reduces Canada in matters of international finance and the influence of the Canadian dollar abroad is practically nil. Is the American dollar practically nil abroad at the present time?

Mr. POPE: The American dollar and the pound sterling are the two mediums of exchange in international transactions.

Mr. McLEAN (*Charlotte*): Why are they?

Mr. POPE: First, because they have acceptance on the part of other countries; by that I mean that smaller countries are prepared to hold sterling or United States dollars as part of their official reserve rather than gold or in addition to gold.

Second, both New York and London offer very professional banking facilities—loan facilities, discount facilities, deposit facilities—which make it a great convenience to use those currencies. As a consequence, it follows that much international trading, exporting and importing, is done on prices based on either pounds sterling or United States dollars.

Now, where this affects us is that we do not buy abroad with Canadian dollars; we do not sell abroad with Canadian dollars; we tend to quote in the



currencies of other countries. Why? Because our dollar is not used abroad; it is not recognized abroad. If there were foreign banks in Montreal or Toronto, a Brussels' importer wishing to deal directly with Canada to obtain Canadian dollars would find it much easier. At present he merely buys American dollars and has the transaction finalized in New York.

Mr. McLEAN (*Charlotte*): The companies I have been associated with practically all my life are dealing with 62 countries at the present time. We sell abroad in Canadian dollars; we also sell abroad in American dollars, and I cannot see that clause 157 makes any difference to us. The reason that the American dollar and the pound sterling are reserve currencies is that they were established by the International Monetary Fund as reserve currencies. One reason that I think France complains all the time is that the franc is not a reserve currency. In my early days London was the settling point, not New York; but as a result of two wars it came to New York, which will remain a settling point. It is only because they have now got their dollar in trouble that they have guidelines. I do not think the American dollar is any better than the Canadian dollar at the present time, when it comes to dealings outside.

Mr. POPE: It was not suggested it was, sir.

Mr. McLEAN (*Charlotte*): It has really become a domestic dollar. I do not see how clause 157 is going to affect the dollar.

Mr. POPE: I suggested this as a secondary effect. It is an insidious little thing. It does not say that foreign banks may not open foreign branches. It says nobody may use the word "bank". Fine, so the Bank of Brussels cannot open a branch in Montreal because it runs afoul of this clause which deals with it.

Mr. McLEAN (*Charlotte*): How can the Bank of Brussels open a branch in Montreal and be controlled by the central bank?

Mr. POPE: Any guest in this country may be controlled. Parliament is supreme, sir.

Mr. McLEAN (*Charlotte*): Then we would have to pass different legislation to make provision for it. We would have to change our central banking system.

Mr. POPE: I am a simple person, sir. I do not see that if the Bank of Brussels or a bank of such repute chose to open a branch in Montreal, to pick the French-speaking half of the axis, that it would be essential that it came under the Bank of Canada's supervision.

Mr. McLEAN (*Charlotte*): Do not some foreign banks now have what could be referred to as banks in this country? Do they not own trust companies which take deposits and give chequing privileges. Are these not fully owned by a foreign bank?

Mr. POPE: I cannot think of a trust company, offhand, other than the subsidiary of the Mercantile Bank; but you are quite correct, sir, in that two Swiss banks with the highest reputation have opened up offices in Montreal and have chosen to name themselves, very carefully, by avoiding the use of the word "bank". But they limit themselves as to what they actually can do.

Mr. McLEAN (*Charlotte*): It is really a fact that international money has no sovereignty and in our Bank Act we are really trying to keep our own sovereignty. International money owes no patriotism to anybody.

Mr. POPE: No, sir.

The CHAIRMAN: Are there any other questions on clause 157?

I would now like to recognize Mr. Cameron, followed by Mr. Lambert and Mr. Clermont.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Pope, I have been wondering why you think our problems will be solved by deleting that aspect of clause 157 which confines the use of the word "bank" to the chartered banks in Canada. At the present time, as I am sure you must know if you have been following the proceedings of this Committee, the Committee has been quite concerned with the operations of near-banks.

Mr. POPE: Quite.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Do you not think that the best way to solve the problem would be to retain the use of the word "bank" but also to have a definition of the word "banking", which we do not have?

Mr. POPE: Are you asking me a question, sir?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes.

Mr. POPE: I must emphasize that I am not a lawyer, sir, but in answer to your question my feeling is that if Parliament ever chose to try to define "banking", a word that has defied the ability of many jurists to define—immediately it froze the meaning of the word by legislation the courts would run into a great deal of trouble. I have been told this by lawyers and I think I am right in the various opinions I have read. Again, I understand from lawyers that the current definition of "banking" is one composed by a jurist, I believe, on the Judicial Committee of the Privy Council in Great Britain, who said in effect that a "banker" is "one who holds himself open to the accepting of deposits and allows a chequing service." "Allows a chequing service" is an addition which perhaps was put on later. As soon as you incorporate such a phrase in legislation and say that from now on this is banking, immediately, ingenious people will find ways of getting around that and doing something which does not quite follow the definition and are, therefore, outside the intent.

By not defining it and merely bearing in mind that the British North America Act already gives you all control over banking, you do not have to define it. Let the judge worry about that if a court case ever comes up.

The CHAIRMAN: Mr. Pope, why is a judge better able to deal with this than the elected representatives of the Canadian people?

Mr. POPE: I did not say that, sir. I am trying to preserve your jurisdiction. I suggested that as soon as you define it, you merely carve a piece out of it and leave fringing areas as you have now. You have a sad situation now that the provincially incorporated trust companies and the provincially incorporated finance companies are considered—I say they are not—to be outside your jurisdiction because of an interpretation of this clause 157. I say that under the B.N.A. Act they belong to you.

The CHAIRMAN: Can you direct us to any decisions where clause 157 has been used to narrow the federal jurisdiction over banking?

Mr. POPE: Precisely, sir. It is common ground today that the provincially incorporated—

The CHAIRMAN: Just a minute. I asked if you could direct us to any decisions of any courts in Canada based on clause 157?

Mr. POPE: No, sir.

The CHAIRMAN: You were saying what might happen.

Mr. POPE: No, sir. I am saying that it is the opinion of Her Majesty's federal government and all Her Majesty's provincial governments that a provincially incorporated trust company does not fall within your jurisdiction even when it engages in banking. This is absurd.

The CHAIRMAN: I did not know that the doors were closed that fully on the other possibility.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Pope I am sure you will agree that it is necessary to have the institutions which are now termed "banks" under the control of the federal government and in their special relationship to the central bank to the reserve system. Do you agree that this is the case?

Mr. POPE: Yes, but I would put it in a slightly different way. I agree that in a country with a central bank, the large commercial banks should be forced to keep reserves with the central bank.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): So that the central bank may have some control of the total money supply at any time?

Mr. POPE: Precisely.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Do you not think that if you removed this restriction on the use of the word "bank", we shall have a rather confused picture in Canada in the eyes of the public, at least, who will not be able to distinguish between the institutions that have to maintain reserves with the central bank and other institutions which have no such obligation at all?

Mr. POPE: I am a great believer in liberty, sir. I believe that somebody having money to deposit in a place of safekeeping should be guided by a good reputation. There is a bank in this country which is celebrating its 150th anniversary about the same time as we are celebrating our 100th anniversary. This bank has a good reputation, and the public should know about it. That would be a good bank to use. If a financial institution was incorporated two years ago and it did not publish a balance sheet, it would be suspect. Indeed, there are normal rules of prudence by which a person guides himself in his financial affairs. In other words, I might answer by asking another question: Is it the role of Parliament to so surround the area of finance with limitations and difficulties that you render the normal workings of honest business difficult in an effort to stop a thief? A thief is going to find a way of stealing no matter what you do, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I must confess I do not see that you are going to gain anything by removing this restriction on the use of the word "bank". As I say, I think you will just add confusion. Rather, I would think that we should be directing our attention to making the assertion of federal authority which you have suggested should be made.



Mr. POPE: I am suggesting that an unfortunate side product of this section is that by implication it very severely limits the authority which Parliament has under the constitution.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But that restriction would be removed if there were a definition of what constitutes a bank.

Mr. POPE: Admittedly, sir, I think this is a dangerous game to play. I think it would result in difficulties in the courts eventually if one tried to define banking. Yes, I really do, sir. In other words, the situation is ideal. The British North America Act allots banking to your responsibility, the responsibility of the federal government. Fine. That is sufficient definition, "banking". That gives you the whole thing.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, but if you do not know what banking is, how do you do this?

Mr. POPE: First of all there is the common sense of the legislators. When they talk about banking they know pretty well what they mean. If the matter goes to the courts, as it has in England, I suggest that leaving it tenuous in this way gives you more scope for proper legislation, more scope for control and more scope for stepping in and saying that this is a bad situation. In banking we will take steps to correct it which, practically speaking, you do not now because so many people have the idea that you only control through the Inspector General the seven or eight banks that we refer to in this country as chartered banks. The practical result of this wretched section is that you only consider yourself responsible for the seven or eight chartered banks and not all the other bankers. Now, I have broken the law because I used the word "bankers" to describe other people.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No, you have not broken the law, but they would if they used it.

I will leave that point just now. I am interested in your suggestion that the use of the word "bank" which has, as you point out, the effect of preventing foreign banking institutions from establishing themselves in Canada, is necessarily a bad thing. I would like to have from you a little more specific information about the more sophisticated banking services to which you refer. I must admit I am inclined to agree with Dr. McLean that apparently Canadian businesses can do business throughout the rest of the world and I really must point out to you again what Dr. McLean pointed out to you, that the position of sterling and the American dollar is as the result of the decision of the International Monetary Fund, a decision taken because of the economic position of those two countries. It does not matter what we do; we could alter our legislation here as much as we liked and the Canadian dollar would not assume that position vis-à-vis the International Monetary Fund. You stress the fact that we do not buy or sell with Canadian dollars and that foreign currencies are not current in Canada, but this is true of every country. The definition of a currency is that it is the only currency that circulates within a political entity.

Mr. POPE: I was making reference to the practice in continental financial centres where cross markets in foreign exchange are made in every European currency. They are not in Canada.

The CHAIRMAN: Are you suggesting that a Canadian bank will not give you a quotation on the Danish krone in Canadian dollars if you asked them for it?

Mr. POPE: They will give it to you, but they do not make the market themselves; they get it from New York and multiply the New York quotation against—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It is not very long ago that I bought Egyptian currency without the slightest difficulty right here in Ottawa.

Mr. POPE: Granted, sir, and perhaps you think I am being very technical, but from my experience I know how they make their quotation. The quotations are obtained by telephoning New York and asking for the rate on Egyptian pounds for that particular day, and they are advised it is such and such. They then multiply that by the Canadian-U.S. dollar rate and then give you a rate. They look at you with a professional eye as if they were experts in Egyptian pounds. They are not; they did not know the rate until they telephoned New York and got the rate.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Is this not because the American dollar—and sterling—now to a lesser extent is the yardstick by which all other currencies are measured?

Mr. POPE: Not in this field of foreign exchange, sir. In Brussels, Paris, Zurich and Geneva there is a proper foreign exchange market working, but not in Montreal or Toronto.

The CHAIRMAN: How do you define a proper foreign exchange market?

Mr. POPE: Where the representative of the bank in the trading department will make a market on his own capital and he has a principal in more than just one currency. In Canada a foreign exchange trader, an employee of the bank, on a trading desk will make a market in U.S. dollars as a principal and on his own risk. He is doing this as an expert and will not get into trouble, he knows what he is doing, he knows the right rate. If you ask him to quote Belgian francs in Canadian dollars or Swiss francs in Canadian dollars he cannot do it. In Switzerland they can.

The CHAIRMAN: What do you mean he cannot do it? You just told us he will give us a quotation.

Mr. POPE: He cannot do it without asking someone else to give him a rate.

Mr. CLERMONT: Mr. Chairman, if an American bank had a branch in Montreal or Toronto, would they not also call their office in New York and ask for a quotation, or do they do their work in Montreal or Toronto?

Mr. POPE: If an American bank had a branch in Montreal today and there was no colony of foreign bank branches in Montreal or Toronto, the answer to your question would be yes. I am suggesting that if there was a colony of foreign banks operating in Canada that you would have a primary market in Canada for foreign exchange which you do not have.

The CHAIRMAN: What is the benefit beyond what we have now?

Mr. POPE: I will give you an example. It might surprise you to know that when we sell wheat to Russia, all the business—by law, as I understand it—has

to be done through a Canadian grain dealer or grain merchant, commodity merchant. The Wheat Board will only deal with these dealers and the Russian buyer sitting in the Chateau Laurier has to buy the wheat from a dealer. The dealer is responsible for buying the wheat from the Wheat Board, finding a train to take it to a port, finding a ship to take it to Russia, and financing over the nine months or until such time as the Russians pay.

I think there are something like 20 to 40 grain merchants in Winnipeg, three of whom are branches of large New York houses. Generally speaking all the business is done, not by the Canadian grain merchants but by the New York grain merchants who maintain three branches in Winnipeg. Why? Because they have better financial facilities open to them. Two years ago, when a large contract came up, the grain merchants in Winnipeg were aware that the last time they had asked their banks to offer them U.S. dollars for nine months the rate was  $5\frac{1}{2}$  or  $5\frac{3}{8}$  per cent or something like that, and they went to the banks and told them that they missed the business the last time because the rate which was quoted was too high and they would like to know what the rate was going to be this time. The Canadian banks sharpened their pencils and quoted to all the grain merchants in Winnipeg that at the rate of  $4\frac{3}{4}$  per cent they would lend American dollars. Every Winnipeg grain dealer toddled up to the Chateau Laurier, knocked on the door of the wheat buying commission and quoted a rate laying down wheat in Vladivostok, or what have you. Then the Russian merely laughed at them and said, "Fine. That all-in price of yours is based on an interest rate over 9 months of  $4\frac{3}{4}$  per cent. Are you not aware that the government of Russia commands a rate in international markets over 9 months of  $4\frac{1}{2}$  per cent? On your way, little boy".

The New York people, having access through their head offices to the more sophisticated international loan market, if you like, quoted their rates based on a loan rate of  $4\frac{1}{2}$  per cent against U.S. dollars and did all the business and our Canadian people did none, because—and I hate to be so blunt—our Canadian banks are not sophisticated in foreign exchange, are not sophisticated in foreign loan rates and are not sophisticated in Euro dollars, and these other things. The wheat deal is a complicated transaction and it goes through a Warsaw bank. The Canadian banks, I suggest in all humility, lack the sophistication to understand these things, to appreciate the risks involved in trying to quote the proper rate. In this case I cited they were out  $\frac{1}{4}$  of one per cent and the result was that not a Canadian grain merchant did any business. It was all done by three large New York houses.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Are you suggesting that if American banks had been established in Canada that the Canadian banks would have gotten the business?

Mr. POPE: I am suggesting that if there was a pool of foreign banks operating branches in the financial axis of Montreal and Toronto that Canadian businessmen would have more facilities, if you like, available to them to enable them to compete on more favourable terms in the international market.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Now, would the same thing apply to transactions with other parts of the non-Communist world?

Mr. POPE: Oh heavens, yes, that is really what I am thinking of more than anything else.



Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You mentioned the Russian deal. It is a closed economy which is insulated from the financial markets of the world in that way.

Mr. POPE: They were offering to pay in American dollars and they wanted to borrow American dollars for nine months.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, but they had their own set rate on it?

Mr. POPE: They were perfectly well aware of their credit standing, the standing of the Moscow Narodniy bank in Warsaw. They were very well aware of the credit standing of the bank, they knew very well that U.S. dollars were available in Europe for that bank at  $4\frac{1}{2}$  per cent and they were not going to pay  $4\frac{3}{4}$  per cent. I suggest that any bank that quoted  $4\frac{3}{4}$  per cent did not know the market.

One can get very technical and complicated on this thing, but another example is there was once a Vancouver exporter who received a tentative order from Tokyo on steel products but he was asked to accept—believe it or not—Siamese account sterling. Naturally he had never heard of Siamese account sterling and so he went to his banker. The banker he approached was the manager of a large branch of a large chartered bank in Vancouver. This manager had never heard of Siamese account sterling and directed the inquiry up the chain. The inquiry eventually reached the Bank of England through the Canadian branch in London that is why it is there, after all, to look after problems like this—of the chartered bank. The Bank of England, sophisticated as they are, knew very well that the Vancouver businessman could do business against Siamese account sterling but they did not particularly want it to happen that way. They knew that legally, properly and ethically it could be done, so they gave an ambiguous answer and the answer they gave was, "We would not approve the transfer of sterling from Siamese account to Canadian accounts". End of answer. The customer in Vancouver was told the transaction could not be done, while that very day it was being done time and time again. Fifty per cent of the world's trade in those days was being done through bilateral sterling, of which Siamese account was merely one example. The business was lost because he was given an ignorant answer. This goes on the whole time. One could multiply and multiply this sort of thing.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Is not your whole argument really based on, to put it bluntly, the incompetence of the Canadian banking system?

Mr. POPE: Very well, sir, I will go along with that. We are incompetent in sophisticated foreign transactions. I would agree.

Mr. McLEAN (*Charlotte*): Mr. Chairman, I have a question. You say that London was a great international?

Mr. POPE: Absolutely, sir; I have great respect for that market.

Mr. McLEAN (*Charlotte*): Well, why did they have to come to the United States to get \$1 billion or so not long ago in order to keep them from devaluing sterling?

Mr. POPE: I believe one should draw a distinction, sir, between knowledge and expertise and one's wealth and the size of one's profit.

Mr. McLEAN (*Charlotte*): It was purely banking. They had so much sterling out that they could not redeem it. It was a banking situation.

Mr. POPE: It was governmental.

Mr. McLEAN (*Charlotte*): Well, it is more or less governmental, but here is London, the great financial centre of the world, and they have to go to New York to get \$1 billion in order to keep sterling afloat. I do not think there is any harm in a Canadian bank going down there to get a little information.

The CHAIRMAN: Dr. McLean, while your question is definitely related to the topic of discussion, it does bring in some broader elements of international financial problems. Do you have further questions, Mr. Cameron? I now recognize Mr. Lambert, followed by Mr. Clermont.

Mr. LAMBERT: Mr. Chairman, my first observation is that while I agree that the act should call for a definition of banking, I do not quite share the fears of Mr. Pope that by defining banking today you will freeze it forever and that therefore the definition of banking could not evolve with the market. There have been attempts such as the case of the Attorney General for Canada versus the Attorney General for Alberta to the Privy Council to freeze the definition of banking back to 1867. The Privy Council, if I may say so, properly rejected that argument by the province of Alberta.

I must confess that I have some difficulty in following the arguments that you have made that clause 157, which is merely to restrict the use of the name "bank" to people who are incorporated or chartered, has had all of these consequences. I regret, Mr. Pope, that I find a certain non sequitur. I do not think that under any possibility could we legislate into being a proper money market.

Mr. POPE: A proper money market?

Mr. LAMBERT: A proper money market.

Mr. POPE: In foreign exchange, sir?

Mr. LAMBERT: Yes, that we could legislate into existence.

Mr. POPE: No, no.

Mr. LAMBERT: This is something that neither—

Mr. POPE: I am suggesting it has been stifled.

Mr. LAMBERT: Well, I am not too sure, because I think one could operate under the name of Credit Suisse, *comptoir d'escompte*, or what have you. Man's ingenuity in devising names has not been limited. If they wanted to they could operate in Montreal or Toronto, but it may be that the conditions of commerce are not such as to warrant the Belgians, say, establishing an agency. The British did come in with Barclay's.

Mr. POPE: That was a chartered bank, sir.

Mr. LAMBERT: Yes, I know, but they came in and they sold it. I am not too sure that by the passing of legislation you could create a proper money market, because then every banana republic could will into existence a money market by the mere passage of legislation. I agree with you that it is unfortunate that we may not have the appropriate money market, and perhaps the lack of expertise

has resulted in the loss of some transactions, but I am not yet persuaded, sir, that the existence of section 157 has been at the root of that.

Mr. POPE: I see what you mean.

Mr. LAMBERT: While one may say, well, the use of "bank", "banking" or "banker"—

Mr. POPE: Barclay's Bank, a bank of the highest reputation, may not open a branch in Montreal or Toronto. That is a direct result of section 157. That is my point there, sir. I would love to see Barclay's bank—

Mr. LAMBERT: Unless it gets a certificate under the Bank Act.

Mr. POPE: It has to be incorporated as a fully owned subsidiary.

Mr. LAMBERT: All right, it can, and this is what we have a right to insist upon if they are going to use those names. It would not prevent Barclay's bank from operating in Montreal through some merchant banker's name, or something of that nature, but I do agree that the lack of definition of "banking" has allowed a lot of, shall we say, "squatter's rights" operation. That is all I can call a lot of the claims of provincial authorities today, that they are pure "squatter's rights" claims with regard to the operations of trust companies and near banks, and they assert the right to regulate them because they had the right to engender them.

Mr. POPE: But I suggest section 157 is a quasi definition, sir. It is a sort of negative definition. He who is not incorporated under this act is not a banker. It is a double negative. Therefore, only he who is incorporated under this act can engage in the business of banking. That is the unfortunate implication. Take this out and then your house returns to order.

Mr. LAMBERT: I disagree with you. I would like to see that section beefed up to give us a definition of banking. If one will look at some of the judicial decisions over the years there are some excellent suggestions by some of the judges as to what could be a very fluid definition of banking, and it is unfortunate that this has not been picked up. I hope we can make some suggestions a little later on.

That is all I am going to say insofar as that is concerned. While I will agree with some of the things that you have said initially, I regret that some of the subsequent paragraphs, as to the non-existence of a money market, are a bit of a non sequitur as far as I am concerned.

(Translation)

Mr. CLERMONT: Mr. Chairman, with regard to Clause 157, Mr. Lambert has just said—and I share his opinion in that connection—that if foreign banks are not established either in Toronto or Montreal, it is because they did not think it in their interest to come and ask the Federal Canadian Parliament for a charter.

Mr. POPE: But do not forget, Sir, that it is not easy to get a charter in Canada. The experience of last year has shown us this. Now, I am offering you, as an instance, a better instance, the way things are done in London. There, there are 200 branches of foreign banks, everybody is happy, things are done in a gentlemanly way and nobody tries to steal anybody else's business. The great English banks are not dissatisfied because there are a great number of foreign banks. They are happy because it is better for business. The situation as it is now



makes it very difficult for a foreign bank to establish itself in Canada. And that is a problem. As you have just suggested, it is not because they do not have the wish to do so. I think it is very hard for them.

Mr. CLERMONT: You say it is very difficult to apply and obtain a charter from the Canadian Parliament. I think that last year we had an instance to the contrary, because Parliament approved two banking charters.

Mr. POPE: Two or one?

Mr. CLERMONT: Two.

Mr. POPE: Yes, but I thought that was three years ago.

Mr. CLERMONT: Did the Bank of British Columbia not get its certificate from Treasury? Parliament did grant permission to two groups to carry on banking operations in Canada. In the United States, the agencies of foreign banks are established mostly in New York and in San Francisco.

Mr. POPE: Those are not branches, they are agencies. Canadian banks do not have the right to accept deposits from New York State residents.

Mr. CLERMONT: But there are branches of foreign banks in the State of New York.

Mr. POPE: I do not know of any.

Mr. CLERMONT: According to the report prepared by a professor there are.

Mr. POPE: These were agencies, Sir.

Mr. CLERMONT: No, these were branches, Sir. An agency established in New York cannot accept deposits from New York State residents.

Mr. POPE: Yes.

Mr. CLERMONT: It can accept deposits from other people, from other residents than those of New York State. I am saying that in the State of New York there are foreign banks that have branches.

Mr. POPE: I do not know of any.

The CHAIRMAN: They were accorded State charters. That is, foreign banks are there only as agencies.

Mr. CLERMONT: I have two cases where the Canadian industry has lost business on account of lack of information furnished by Canadian banks in connection with exchange. Are the two instances you mentioned, Sir, a matter of personal experience or things that were reported to you?

Mr. POPE: A matter of personal experience.

Mr. CLERMONT: Because you mentioned that, among others, our grain brokers landed at the Chateau Laurier and said: "It is very regrettable, you are good boys—

Mr. POPE: I was in contact with both sides. I was trying to find cheaper money than 4½ myself as an agent. And that is why I know what I am talking about in that case. I offered money at 4½ per cent in Winnipeg.

Mr. CLERMONT: Are you familiar with the other cases besides the two you mentioned? Because these were very important transactions.

Mr. POPE: In the case of Winnipeg and the wheat exports, I myself offered to the wheat dealers in Winnipeg money at  $4\frac{3}{8}\%$ . I offered a better rate than the banks did, because I can get money at  $4\frac{1}{2}\%$  per cent. I did not want to say that at the outset but to show how I was aware of the situation, I was able to obtain this money at  $4\frac{3}{8}\%$ , whereas the Canadian banks would have insisted on  $4\frac{3}{4}\%$  per cent.

Mr. CLERMONT: So you say—

The CHAIRMAN: But this did not prevent you from offering American money?

Mr. POPE: No, Sir.

The CHAIRMAN: How did Clause 157 prevent foreign banks from doing business in the same way here as you did?

(English)

Mr. POPE: The point, Mr. Chairman, is that as a lone wolf money operator I was able to offer money to Winnipeg grain dealers at a rate of one-eighth of one per cent cheaper than their own banks were offering it to them. But this rate, sir, was not competitive. In other words, I was not even able to be competitive myself, and my suggestion is that if we had a nucleus of perhaps half a dozen foreign banks operating in here the market would be the right market and the rates would be the proper rates.

The CHAIRMAN: I was just going to say my point—and I believe Mr. Clermont laid the groundwork for this—was that if you, as a private entity, were able to do this in spite of section 157, I find it difficult to see what would prevent a group of these foreign banks from operating in Canada at the present time as entities—not calling themselves banks—in spite of section 157, and doing what you are doing in an even more favourable way because of their greater resources.

Mr. POPE: The proof of the pudding is that I did not succeed.

The CHAIRMAN: No, but my point is that apparently section 157 would not have prevented the foreign banks from doing the same thing as yourself and making a better rate because of their greater resources and know-how. What I am trying to say, sir, is that you yourself seem to have offered as evidence the fact that section 157 is not creating the evil that you claim. This is from your own personal experience, you have just told us about it.

(Translation)

Mr. CLERMONT: Instead of striking out clause 157—Mr. Pope, would it not be preferable, according to your judgment, for Parliament to adopt an Act permitting the establishment of agencies with some restrictions.

Mr. POPE: This would be a great improvement on the situation as it now stands. I think I would prefer to see branches rather than agencies. Even agencies would be a great improvement, however. Now we have nothing.

Mr. CLERMONT: You mentioned at certain times the London market. Are foreign banks in Great Britain distributed throughout England or just established in London?

Mr. POPE: There are no branches outside of London as far as I know.

Mr. CLERMONT: Are they interested in obtaining deposits from the public, or just in currency and foreign exchange transactions?

Mr. POPE: I think that they are free to receive deposits from anyone in London.

Mr. CLERMONT: Is it the intention of these foreign banks to go in for deposits or are they only concerned with foreign exchange?

Mr. POPE: I do not understand your question, Sir.

There are perhaps some 200 foreign branches in London. They are there for the business of their countries. For instance, the Bank of Montreal, to give you an instance, because I was an employee of the Bank of Montreal; the Bank of Montreal has two branches in London. They have one in the centre of London for Canadian tourists; who are clients of the Bank of Montreal they do all their business there; they buy sterling and so forth, and there is another branch, in the financial City, for the big financial operations, between Canada and Great Britain. It is essential for the Bank of Montreal—to have branches in London. The Bank of Montreal, the Royal Bank, the Bank of Nova Scotia would be very embarrassed if the laws of Great Britain prevented their having branches in London. Everyone wants to have a bank there. The point is that the great English banks are not dissatisfied with their situation because all these foreign banks bring business for everybody. I have the impression, some people have the feeling that Canadian banks fear competition.

Mr. CLERMONT: But, Mr. Pope, to date there are two banks with foreign capital who have asked the Canadian Parliament for a charter—the Mercantile Bank and the Barclay's Bank. I do not think Barclay's Bank established many branches throughout the country. Now they are merged with another Canadian bank.

Mr. POPE: But they selected the difficult road. Because the Act did not allow branches, they opened chartered banks. But once they had chartered banks, they became Canadian banks. Now they can do what other banks can do. Barclay's Bank opened four or five branches; the Mercantile Bank opened some six or seven.

Mr. CLERMONT: Mr. Chairman, I revert to the first question I asked Mr. Pope. I think, personally, that if foreign banks did not judge it feasible to ask the Canadian Government for a charter, it was because it was not in their interests or in the interests of their countries to come and settle in Canada.

Mr. POPE: You are asking a question?

Mr. CLERMONT: Yes.

Mr. POPE: That is not my opinion, Sir. My opinion is rather that to open a bank—there are things a bank has to do and the various proceedings are so difficult for a foreign bank to open in Canada and get a charter from Parliament that they just do not bother to do so.

Mr. CLERMONT: But you mention London. You do not mention the United States. It is not easy for a Canadian bank to set up branches in the United States.



Mr. POPE: I do not approve of the American system. I am just giving you the London instance as an example which is the primary example of how to do banking business.

Mr. CLERMONT: But you admitted in answering a question from Dr. McLean (Charlotte) that the world market is presently in New York.

Mr. POPE: No I did not say that, Sir. The American are not the bankers. The Londoners are. The fact that the sterling is as weak as it is now, and that they had to borrow a billion in New York, in their weakened state, does not change matters. It is on account of their expertise that the market remains in London, and not in New York, and just for that.

(English)

The CHAIRMAN: Do we have further questions? Mr. Gilbert? We are dealing with section 157 and Mr. Pope's views about its effects.

Mr. GILBERT: Mr. Pope, I understand that you want to strike out section 157, and at the same time you do not want to define banking.

Mr. POPE: That is right, sir.

Mr. GILBERT: Is it desirable that the federal government exercise jurisdiction over finance companies and near banks, and so forth?

Mr. POPE: That is a loaded question, sir. My point is this, sir, that under the constitution you, the federal parliament, has jurisdiction over banking; that cannot be taken away from you. It is part of my presentation that this section be taken out completely, and as far as that part of the question concerning near banks is concerned that in as much as banking comes under your jurisdiction then, *ipso facto*, that responsibility is yours.

Mr. GILBERT: Let us get a direct example with regard to finance companies. Let us take the case of Prudential Finance.

Mr. POPE: Yes, sir.

Mr. GILBERT: They have a collapse and the Minister of Finance says, "it is not within my jurisdiction, it is provincial jurisdiction".

Mr. POPE: May I ask the question whether he did or not?

Mr. GILBERT: He did.

Mr. POPE: He did?

Mr. GILBERT: Yes, he did. He said it was provincially incorporated and the only responsibility we had was with regard to federal—

Mr. POPE: That is my point, sir. The unfortunate implication of section 157 is that a minister can get up in the House of Commons and say, "Prudential Finance"—which we all know is engaged in banking—"does not come under my jurisdiction".

Some hon. MEMBERS: No, no.

Mr. POPE: The unfortunate implication is that the Minister of Finance can get up in the House of Commons and say, "This is a provincially incorporated company; it does not fall within our jurisdiction". But Prudential Finance was engaged in the business of banking.

Mr. GILBERT: Well, was it? That is the question. The question is was Prudential Finance in the business of banking?

Mr. POPE: Prudential Finance was doing most of its financing through the sale of notes. If that was all that it did that would take it out of banking, but I believe they also accepted demand deposits, sir.

Mr. GILBERT: No, not to our knowledge.

Mr. POPE: Not to your knowledge?

Some hon. MEMBERS: No.

Mr. POPE: Well then, I am wrong and I withdraw on Prudential.

Mr. GILBERT: And I do not think they provided chequeing facilities either.

Mr. POPE: No, they did not provide chequeing facilities but I did believe that they took some deposits.

Mr. GILBERT: All I am saying to you is that in the absence of a definition you have these practical problems like Prudential Finance, where the federal government does not assert its jurisdiction.

Mr. POPE: If I may make the suggestion, Sir, it depends a great deal on the personality of the responsible member of the cabinet. A strong man would say, "Everything is banking. It is all mine. I do not care what you say, I am acting. Let the courts fight me if they wish". A weak man will take less responsibility and limit the vista of his own responsibility. This, I suggest, is a psychological problem, sir.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): May I ask a supplementary question?

The CHAIRMAN: Certainly.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would you not agree that if a minister were prepared to do this—which I submit would be rather rash of him—would he not have to have some argumentation on which to base his action and would that argumentation not, in the final analysis, have to be based on a definition of banking?

Mr. POPE: In the final analysis, yes, sir. The minister to justify himself would merely say, "This is banking. I will chop your head off if you are a bad banker".

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): He would have to have some basis for his decision, surely.

The CHAIRMAN: What Mr. Cameron is trying to say, supported by Mr. More and Mr. Gilbert, is that the Minister of Finance cannot act like the first chancellors in Britain when they started the equity system and they defined equity as being the length of the lord chancellor's foot. We have evolved since then and the minister's views have to be based on the law, either as declared by parliament in legislation or on a decision by the courts.

Mr. POPE: I think the courts would have some decisions pretty quickly.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): There is also the other point, Mr. Pope; how would he exercise his authority?

Mr. POPE: This is wide open, sir, to parliament. Parliament has the responsibility over matters of banking. Therefore it is up to parliament to set up whatever boards or control commissions, or what have you, to supervise these matters. Parliament is supreme in these matters.

Mr. GILBERT: Do you think the same would apply to Caisse Populaire and credit unions?

Mr. POPE: Caisse Populaires are definitely banks, there is no question about it.

Mr. GILBERT: And the same with regard to credit unions?

Mr. POPE: Credit unions in my mind are the same thing as Caisse Populaires.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Well then, if the Minister of Finance were to exert his authority, I presume it would have to be based on existing legislation, would it not?

Mr. POPE: Well, you are asking me to imagine a situation in which the minister would exercise certain authority in a case where he thought something was beginning to be rotten in the state of Denmark.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No, not necessarily rotten in the state of Denmark, but where it might become rotten.

Mr. POPE: Where it might become rotten. Fair enough. Now, at the present time, sir, the only organization that has been set up to my knowledge is that of the Inspector General of Banks and I believe a certain little legal section in the Treasury. They are the only two that I know of, but an ingenious minister could expand those very quickly. If he did not want to expand them, parliament could make him do so; parliament is supreme.

The CHAIRMAN: Did you ever hear about the difficulties in getting anything approved by Treasury Board? You say an ingenious minister could expand. I presume you mean the establishment; hiring people and opening offices. There are some ministers who would like to expand their establishments who would give you quite an argument about that.

Mr. POPE: Well, if I were the Minister of Finance and I did not like a little smell that was brewing in one of our cities, I would telephone my inspector general and have him look into it.

(Translation)

Mr. CLERMONT: On what would the Minister of Finance base himself to interfere in the operations of a company which had a provincial charter? Even if he is a strong-willed minister, or a dictator?

Mr. POPE: I never said dictator.

Mr. CLERMONT: You said . . . and the gesture you made . . .

Mr. POPE: Any provincial government has a right to create incorporated companies. If these creatures carry on banking operations, their operations fall under the jurisdiction of the Federal Parliament, while being the creatures under the provincial government.



(English)

The CHAIRMAN: I think what the Committee is trying to get at is this: you are merely suggesting to the Committee that section 157 be swept away, without simultaneously placing in legislation not only a definition of banking but authority for an administrative apparatus to supervise and investigate generally the other institutions you define as banking. You have not called for that and I would think, sir, that even if one was willing to accept your interpretation of the evil effect of section 157, it would be difficult to see—and if I may summarize what the Committee, I think, is trying to get at—how the situation would be improved with respect to supervision over what you define as banking without adding other clauses to the law to give a minister authority to do something. To take a practical example, if the Inspector General of Banking had turned up at the door of Prudential Finance six months ago and the manager of Prudential Finance said to him, “Would you kindly show me under what authority you want to look at my books, what legislative authority do you have to look at my books?” what answer would the Inspector General have been able to give?

Mr. POPE: I am not a lawyer, sir, nor am I a Member of Parliament. I am pointing out a problem that I suggest is the result of clause 157. I am, perhaps, pointing out something that you gentlemen are becoming aware of, which is that there are things going on that really should be more under your supervision than they have been. I did not want to say it but you force me to say it. I have been trying all morning to avoid making such a remark.

The CHAIRMAN: We do not mind that, because many of us have been thinking along those lines for some time.

Mr. POPE: Yes; that is why I dared to say it. But there are other countries in the world that have met the same problem, sir. I am not a lawyer, but either Parliament passes a statute setting up a board of administration, or a board of supervision, on matters of banking, or the legal advisers decide that the present legislation is sufficient; that the B.N.A. Act is sufficient authority for the Treasury Board or the Minister of Finance to set up his own commission.

Mr. LAFLAMME: How can we do that without having a definition of what are matters of banking.

Mr. POPE: I suggest, my dear sir, that for the time being one assumes that the commonsense interpretation of “banker” is “taker of deposits payable on demand.”

The CHAIRMAN: What is wrong with writing that into the law.

Mr. POPE: I am not a lawyer, and I insist that I am not a lawyer, but I am afraid, as I have been advised by lawyers, that if one did that one would run into trouble. I am relying on my legal opinions.

The CHAIRMAN: As a lawyer I should point out that one should always be conscious of the advice of lawyers, given off the cuff.

Mr. POPE: You asked me to draw the picture. I am afraid that as soon as you circumscribe banking, as this wretched clause does in a double negative, you will again have fringe operators saying, “I am outside your legislation. Leave me alone”. It is silly to define it if you have that.

Mr. LAFLAMME: Mr. Chairman, it is on that question that I have a supplementary to ask.

Mr. GILBERT: I think Mr. Lambert may have asked you this question. You still want to have the provincial governments retain jurisdiction with regard to incorporation of these financial institutions. Why?

Mr. POPE: No; I did not say that, and I gave no opinion on that, but I will now give this opinion, that if the federal parliament pointed out to the provincial parliament that it had no business whatsoever incorporating banking children, I would say that you would be in the right. I would say that you would be in the right, and therefore, the Royal Trust and the Montreal Trust would pass out of existence tomorrow morning, if you ever took that step. The point is that it is an interesting little door that we open there. It could be argued possibly that a provincial parliament has no authority for incorporating the banking infant—creating the banking child; but it could be argued that they could create anything.

The CHAIRMAN: I should just interject that I doubt very much that if a court ruled that the provincial parliament did not have this authority their previous creations would suddenly go out of existence. Since this is a public hearing, and these remarks are being recorded both for our own minutes and by the press, I think we should cast some doubt on your suggestion that these entities would suddenly go out of existence.

Mr. POPE: I would be happy to withdraw the remark and point out that it was said very much in the spirit of jest.

Mr. LAFLAMME: May I ask Mr. Pope another question? Do you accept the principle that the central bank must control credit?

Mr. POPE: Absolutely.

Mr. LAFLAMME: You do; and while doing so, if we remove the definition in Clause 157 for your purpose, to allow some other banks to do banking business here in Canada without being under the control of the Central bank, how could this principle apply?

Mr. POPE: There are two ways, sir. First of all, any foreign bank opening a branch in Montreal or Toronto could be required to keep a certain percentage of its deposits with the central bank. This is no problem at all. Secondly, the deposits of a few foreign banks having branches in Montreal or Toronto would be so small in relation to the deposits of the banking system as a whole that the Bank of Canada's influence would hardly be affected; the loss of influence would be miniscule because of that. It would be a simple matter to require that these banks keep on deposit with the Bank of Canada the same percentage of their deposits as the chartered banks are required to do. This is no problem, sir.

The CHAIRMAN: I will accept a supplementary question from Mr. Lambert.

Mr. LAMBERT: If you were to allow foreign banks to come in and operate for the purposes of a money market and if you were to allow the development of private bankers, would you not agree that it would be essential that they be under the supervision of the superintendent of banking in all of their operations?

Mr. POPE: I think I would agree with that.

Mr. LAMBERT: Private bankers, as well.

Mr. POPE: I think I would agree with that, yes, sir.

Mr. LAMBERT: Although perhaps not in the same degree as the chartered banks operating on the branch basis today.

Mr. POPE: I think I would agree with that. I would love to see a return to private banking. I think it is sadly lacking here.

Mr. LAMBERT: Thank you.

The CHAIRMAN: Do we have any further questions? Yes, Mr. More?

Mr. MORE (*Regina City*): Mr. Chairman, I would like to ask Mr. Pope about money markets. As I understood it, he did not appreciate the American restriction and system in regard to foreign banks, yet this has not stopped New York from becoming a money market.

Mr. POPE: In an imperfect way, sir. They have possibly as many agencies in New York as there are banks in London. It has not stopped New York from becoming a money market, as you say quite correctly, sir; but I emphasize very, very strongly my feeling that New York is not by any means a complete money market in the sense that London is. They have an imperfect system, sir.

I have high standards.

Mr. McLEAN (*Charlotte*): Mr. Chairman, I have just one question. The Russians have always had a bank in London, under both the Czar and the communists, have they not?

Mr. POPE: I have a feeling that the present bank—

Mr. McLEAN (*Charlotte*): They also lend money to England. I suppose they take deposits; they lend money there. Why did this Russian deal that went through the United States not go through their own bank in London?

Mr. POPE: It did not go through the United States, sir; it went through a Polish bank in Warsaw.

Mr. McLEAN (*Charlotte*): Why a Polish bank, when they have their own bank in London?

Mr. POPE: That would be the agency—

Mr. McLEAN (*Charlotte*): Why, if London is the big financial centre and they have a bank there and have had ever since the time of the Czars?

Mr. POPE: I am not saying the money did not come from London, sir. I am merely saying that the credit that was offered to the people selling the wheat was the credit of a government-sponsored bank in Warsaw. That is the technique they used. The money was raised either in New York, London or Zurich.

Mr. McLEAN (*Charlotte*): What did the Russians pay with?

Mr. POPE: American dollars.

Mr. McLEAN (*Charlotte*): I understand they paid with 500 million in gold.

Mr. POPE: They sold gold to buy dollars, and with the dollars—

Mr. McLEAN (*Charlotte*): American dollars?

Mr. POPE: American dollars; I am sorry.



Mr. McLEAN (*Charlotte*): And they ended up in New York.

Mr. POPE: The deal was done against American dollars.

The CHAIRMAN: Mr. Lind?

Mr. LIND: Returning to Mr. Pope's opinion on the authority of the federal Minister of Finance, has he the right under the present legislation to investigate and regulate a provincially-incorporated company?

Mr. POPE: As I say, that is a legal question sir; I do not really feel qualified to answer it.

Mr. LIND: Well, you made the statement a little while ago that the Minister of Finance could have stepped in and controlled the Prudential Finance Corporation.

An hon. MEMBER: He withdrew that statement.

Mr. LIND: Pardon?

An hon. MEMBER: He withdrew that statement.

The CHAIRMAN: I think, in fairness, we should not try and impose upon Mr. Pope an obligation to deal with questions he does not consider himself qualified to answer.

Mr. POPE: I have been suggesting during my remarks, sir, that all matters of banking fall under the control of the federal parliament. You asked me whether or not the Minister of Finance had the power to do such-and-such a thing. I cannot answer, because I do not know what power parliament has given to the Minister of Finance. That is why I am not able to answer your question.

Mr. LIND: Then how do you come to the conclusion that the Prudential Finance company is in any way a bank? They do not take deposits; they do not issue cheques, or have checking accounts.

Mr. POPE: They do not have checking accounts, no. Their main solicitation of funds was through the sale of notes, which would take them out of banking. I did understand—and I have been corrected by various honourable and learned members of this Committee—that they also took deposits. I am told that that is not the case. Therefore, I think we can conclude, that being the case, that they were not in the business of banking. Therefore, they would not have fallen under federal Parliament supervision.

Mr. LIND: Whose jurisdiction did they fall under?

Mr. POPE: The attorney general, or anybody who is responsible for catching thieves.

Mr. LIND: Well, now, would you explain that answer a little?

Mr. POPE: Yes, sir. We are in a difficult area. It is naturally always the desire of legislators to make it difficult for people to be taken advantage of, or for people to suffer hardship. In other words, it is always the desire of the legislator to protect the public. Because of this desire, the legislators tried to pass laws making it impossible for certain crimes to be committed. I suggest, gentlemen, when it comes to theft, that you can pass all the laws you like, but you will never stop a thief from being genius enough to steal from another citizen.

An hon. MEMBER: Is it worth trying!

Mr. POPE: It is a balance very hard to strike. Unfortunately, much of the legislation aimed at harnessing the efforts of thieves makes it very difficult for honest men to do good business.

The CHAIRMAN: Are you suggesting, for example, that our present legislation, imposing on the chartered banks the obligation to be supervised by the inspector general of banking, makes it difficult for them, as honest businessmen, to do business?

Mr. POPE: No. I believe that the supervision is very benign and paternalistic; it is not oppressive in the slightest.

Mr. LIND: To follow up this question of thieving—and I am not sure that it was thieving, or what it was—you leave the impression that it is purely the responsibility of the attorney general of Ontario to look into this and lay charges if there was thieving. Is that right?

Mr. POPE: That is my personal opinion in this particular case, yes, sir.

Mr. LIND: Then it has nothing to do with the federal Minister of Finance.

Mr. POPE: That is my opinion of this moment, yes, sir.

Mr. LIND: Thank you very much.

The CHAIRMAN: Now may I ask something just briefly before we proceed further?

You have made some very interesting and, I think, quite helpful points with respect to your analysis of the present operations of the foreign exchange market in Canada, and of the operations of Canadian banks. At the same time we all notice advertisements by our Canadian banks showing all the foreign branches they maintain, the foreign agencies, their sources of information in international trade, and so on. In comparison with a lot of banks in the United States and Great Britain we seem to be equally active with respect to opening offices abroad and so on. How is this consistent with your suggestion about our Canadian banks being provincial in the international field?

Mr. POPE: They are certainly very much less provincial than the small banks in the United States, who are "the end" so far as that is concerned. Under the American system where you are not allowed the branch-banking system you have the ultimate in provincialism and lack of proper understanding of banking. The United States is "the end" so far as that is concerned.

The system in Canada, as you point out, is superior to that of the United States, but in my opinion it still leaves much to be desired. A lot of the things you describe are merely advertised as propaganda for public relations.

The CHAIRMAN: Do you mean that they do not have the branches they are advertising?

Mr. POPE: They have the branches they are advertising, sir, but the implication is that they are experts in foreign matters. They are not. They fail our Canadian businessmen—and that I hold strongly.

The CHAIRMAN: Well, because of your own background that is a very helpful and useful suggestion.

I have one further point which has already been raised at least in part. You will agree, will you not, that the removal of this clause will not automatically lead to the creation of the foreign exchange markets and so on which you feel are desirable.

Mr. POPE: I feel, sir, that it removes one obstacle, at least.

The CHAIRMAN: The removal of clause 157 will not alter the fact that Canada is a nation of 20 million, and neither Montreal or Toronto are, in the foreseeable future, unfortunately, the equivalents of New York and London in the world's financial markets.

Mr. POPE: I am hoping that perhaps we might become the equivalent of Brussels which has three British banks, two American banks, four French banks, two Italian banks and one Japanese bank—a total of 12. These figures are four years old, and there might be 15 or 20 by now. But if Brussels, which is half the size of Montreal, can have 12 foreign branches serving it, I do not see why we should be deprived of even one.

The CHAIRMAN: That is a useful suggestion, but as many members of the Committee have attempted to point out to you, some of them find it difficult to see how clause 157 by itself has either prevented this situation from arising, or how its removal will necessarily bring the branches here.

Let us now move on to the next clause.

I do not think, in fairness to our witness, that we will invite questions on what he has had to say about subclause (g) of clause 75, in view of his very reasonable and fair reservation with respect to his own background in this area.

I will invite questions on his views with respect to subclause (2) of clause 53, in the course of which he criticizes the proposal of the government limiting to 10 per cent the shares which may be held by others in a chartered bank.

*(Translation)*

Mr. Laflamme, do you have a question?

Mr. LAFLAMME: On this clause 53, I would like to know the main reasons why you object to the limiting of personal control on a bank.

Mr. POPE: First it removes a certain freedom from the individual. No citizen may now buy up to 11 per cent in Canadian bankshares.

*(English)*

The CHAIRMAN: Also, every person has the right, if he is poor, not to have to sleep under a bridge and be arrested for vagrancy.

Mr. POPE: The point is that you are depriving a citizen of his normal liberty.

*(Translation)*

That is in principle. Generally speaking, the true result is that there is no longer the shareholder control in the bank but management control. All Canadian banks are controlled not by the owners but by management.

Mr. LAFLAMME: We are going to hear a brief this afternoon which is going to contradict that point and insist on the point that we should prevent a group of individuals from dominating—



Mr. POPE: Take the current instance of the Bank of Canada which has just been incorporated, I think that 30 per cent of its shares belong to a group. Now the idea of this bank, is that this is only fair since it is this group which has worked and raised the money required—

Mr. LAFLAMME: But let us speak of the present situation.

Mr. POPE: —say 50 per cent at the present time.

Mr. LAFLAMME: Is it not so, that approximately three Canadian banks chartered banks control an important portion of business generally.

Mr. POPE: This is certainly true that three Canadian banks handle the greater portion of the Canadian depositors.

Mr. LAFLAMME: In this particular circumstance, is it not necessary to establish limitations on individual or corporate participation in the banking business?

Mr. POPE: I think you refer to something that is not so.

Mr. LAFLAMME: But it is so.

Mr. POPE: In three banks you speak of, no one controls 10 per cent.

Mr. LAFLAMME: They control a great deal more.

Mr. POPE: No, sir, no one has a controlling 10 per cent in the Bank of Montreal, the Royal Bank, the Bank of Commerce, or the Bank of Nova Scotia. No one controls them as far as I know.

Mr. LAFLAMME: Let us not speak of individuals, let us speak of interest groups. For instance, I have seen a phrase here.

Mr. POPE: I think I know what you are talking of, Sir. I think this article states that in too many cases, the administrators are the same in all banks.

*(English)*

Mr. LAFLAMME: Just a minute; it was stated here by someone else, that, as is well known, three of the Canadian chartered banks control 70 per cent of the assets of the Canadian chartered banking system.

Mr. POPE: That is right.

Mr. LAFLAMME: Do you accept that?

Mr. POPE: That is true.

Mr. LAFLAMME: Yes, it is true; but do you accept that as a good thing?

Mr. POPE: I have nothing against large size, sir. There three banks are admirable banks. They do their work very, very well.

Mr. LAFLAMME: I agree with that.

Mr. POPE: They are banks that are good, honest banks. They render good service. The fact that they control 70 per cent of the deposits of the Canadian chartered banks is not to me, an evil in itself, sir.

If we are talking about control, I do not know who controls these banks. I have tried to find out. The conclusion I have been forced to come to is that the shareholders do not exercise their control in the case of these three banks and,

therefore, by default, the control falls back on the management itself. The employee becomes the owner, and that is ridiculous.

Mr. LAFLAMME: Do you say that the shareholders do not control at all?

Mr. POPE: I do, sir. They do not exercise their control in the case of these three banks.

Mr. LAFLAMME: But do you not think that a clause which would limit the possibility of controlling any bank is not a good one, in those circumstances?

Mr. POPE: I am trying to keep my thoughts straight. In the case of the three banks, nobody controls them at all, to my knowledge. The shareholders do not exercise their control.

In the case of the three smallest banks one group controls practically all the shares. That is the situation today.

I may be missing your point, sir. In the case of the three largest banks nobody controls them. In effect, the only control is exercised by the management from the general manager down.

Mr. LAFLAMME: That is all, Mr. Chairman.

Mr. McLEAN (*Charlotte*): Mr. Pope, you seem to be disturbed that management has control of the banks. I think it is a good thing that it has control. I do not know why you take—

Mr. POPE: There is a certain amount of inbreeding going on.

Mr. McLEAN (*Charlotte*): You say that this 10 per cent should be raised to perhaps 25 per cent, or something like that, for the individual owner. The large banks have millions of shares. If a bank is worth \$6 billion and a man owns 25 per cent of the shares, he has the actual control of that bank. If you get 25 per cent control of a large company you can actually direct it and control it.

Mr. POPE: That is right, sir.

Mr. McLEAN (*Charlotte*): I think the 10 per cent is a good thing. We do not want anybody controlling \$6, \$8, \$10 or \$15 billion. We want that in the hands of the management. Management is responsible to the stockholders and when they present a good balance sheet the stockholders are quite happy with their continuing on and paying normal dividends, and so on.

I do not see that taking it out of the hands of management would help things. I think it would hurt things.

Many large American companies are controlled by an individual who has 25 per cent of the ownership.

Mr. POPE: Quite.

Mr. McLEAN (*Charlotte*): Then a man, or a group of people, who has 25 per cent of the shares in one bank would control \$6 or \$7 billion. I do not think that is a good thing. I do not see how you can think it is a good thing.

Mr. POPE: You do not think it is a good thing for one man to control so much?

Mr. McLEAN (*Charlotte*): No; I do not think any group should control that much.

Mr. POPE: Actually, the management group does control it all.

Mr. McLEAN (*Charlotte*): If they had control of the three banks they would practically control the country. I think it is better in the hands of management.

The CHAIRMAN: In other words, you are suggesting to us that it would not be in the public interest if it were possible for one individual, or for a group of associated individuals, to share ownership, and to own, possibly, at the same time, two, or three, or even one, of our major chartered banks?

Mr. POPE: You would have to be very rich to acquire such a holding of shares.

Mr. McLEAN (*Charlotte*): It is possible.

Mr. POPE: It is a possibility, yes, sir.

You are arguing, gentlemen, if I might make the suggestion, the possibility of evils if this happened in the three largest banks and, therefore, that it is right to restrict ownership to 10 per cent in those banks. But look at the inconvenience and hardship you put on the proprietors of shares of small banks. The Bank of Western Canada is I think, 60 per cent controlled by the British International Finance Company. They are being forced, under this legislation, to divest themselves of 40 per cent of those shares over the next 10 years. For what purpose? They are a tiny little bank.

(*Translation*)

Mr. CLERMONT: A supplementary question. When the provisional directors presented their application to the Board they were informed of this restriction and they accepted.

Mr. POPE: I agree, but I think nevertheless it makes things unnecessarily difficult for them. They are small banks.

(*English*)

The CHAIRMAN: Are there any further questions on this proposal? Mr. Clermont?

(*Translation*)

Mr. CLERMONT: The present Act has no limitations on percentage I believe, and if I understand you think that it is the management or directors that are running things now?

Mr. POPE: No, not in the large banks. Not the administrators, nor the directors, but the employees. The General Manager the assistant General Manager and all the people that come under him, not the directors. In most cases the directors are the children of the general managers.

Mr. CLERMONT: But what change would Bill C-222 make in regard to the 10 per cent?

Mr. POPE: Nothing would change at all, nothing would be changed. I am against it on principle only.

Mr. CLERMONT: Yesterday I was looking over the list of the directors of the Bank of Montreal. I only know two or three of them, but your reflection that they are children...



Mr. POPE: They do not direct the Bank of Montreal. They are given facts and they say yes or no. It is the general manager and the president who controls the Bank of Montreal.

Mr. CLERMONT: What difference would the limitation bring?

Mr. POPE: They do not exert their control in the bank as ownership I assure you.

Mr. CLERMONT: I see the difference between the limitation of 10 per cent and no limitations as the Act really says right now. You object to the 10 per cent limitation.

Mr. POPE: I object on principle. I think it is a restriction on the individual's liberty.

Mr. CLERMONT: Do you not fear to a great extent the abuse that would come from an associated group that would hold 25 to 40 percent? Or 50 per cent Or 100?

Mr. POPE: Actually, I am not afraid of that. I do not see that this would happen. We can have nightmares about all sorts of possibilities about things that never happen.

Mr. CLERMONT: But as the present Act now stands, we have the case of banks which obtained a charter from Parliament. It was controlled by Netherlands interest. Now it is American-controlled to the extent of 100 percent. That is a case in point.

Mr. POPE: Is it as bad as all that?

Mr. CLERMONT: Some people consider that this is not in the interest of Canada.

Mr. POPE: They have deposits of 225 million dollars, that is not a very great amount.

The CHAIRMAN: Have we any other questions on the suggestions of Mr. Pope? Then we can go over to his next point in regard to the rate of interest. Do we have any questions on his ideas with regard to the rate of interest?

Mr. POPE: You mean the suggested system?

Mr. CLERMONT: Mr. Pope, if Bill C-222 were adopted as it is presently, would you have any comments to make with regard to the rate of interest?

Mr. POPE: Ninety-one do you say? I think it is clause 91(3) establishing a possibility—

I think this would be an improvement on the present system. I am for complete freedom. My personal opinion is that Clause 91, as it is now drawn up is just a compromise.

Mr. CLERMONT: You would prefer that the ceiling be removed at once that there would be no ceiling?

Mr. POPE: Yes.

Mr. CLERMONT: But would this be practical in the present situation when there is a lack of shortage of money, not only in Canada but throughout the world?

Mr. POPE: Nevertheless one must not forget that the great chartered banks know their duties to the public.

Mr. CLERMONT: I admit this, Mr. Pope, but they told us they were in business to make a profit. Here there are no limitations. They are good citizens but profit is very interesting.

Mr. POPE: That is my opinion, sir, I am not afraid of any injustice in this respect.

Mr. CLERMONT: But do you think, sir, that Clause 91 in your opinion is an improvement.

Mr. POPE: Certainly.

(English)

The CHAIRMAN: Mr. Gilbert, have you a question?

Mr. GILBERT: Do you think we should define the word "interest"?

Mr. POPE: I do not understand the question. To me, the meaning of the word "interest" is so evident that I do not understand your question, sir.

Mr. GILBERT: A great deal of our discussion has been on this question of interest and the definition of what constitutes interest.

Mr. POPE: Really? I was not aware of this, sir.

The CHAIRMAN: Without taking too much time, in other words, Mr. Gilbert is referring to the fact that borrowers face various charges in addition to what is commonly referred to as interest.

Mr. POPE: I see. In other words, you are suggesting that because a law could be passed regarding interest, then a clever lender can say, "fine; I am charging you a bonus."

I would merely make the comment that it would take a very ingenious legislator to get around all the possibilities.

I have no real comment to make, sir. I still do not quite understand your question.

Mr. GILBERT: In the present Act we have the 6 per cent ceiling.

Mr. POPE: In the Bank Act, yes.

Mr. GILBERT: Consumer loans are at 11 per cent, which includes—

Mr. POPE: In the banking system?

Mr. GILBERT: In the banking system; if you go to the bank and you ask for a personal loan...

Mr. POPE: A personal loan is at 11 per cent, in spite of the 6 per cent ceiling; that is right; because of a different interpretation.

Mr. GILBERT: That is right.

Mr. POPE: Because of legal advice that the banks have received.

Mr. GILBERT: I am asking you: Should we have a clear definition on that?

Mr. POPE: I think you are referring to the section of the Bank Act which refers to 6 per cent interest and 6 per cent discount, and I suggest it is not

merely a definition of "interest", but a definition of how to apply the discount. I think that the whole loophole that counsel for the banks found was in the word "discount". In other words, to take the simple example of borrowing \$100 for one year, repayable at the end of 12 months: Under simple interest you pay back \$100 at the end of the year, plus \$6 interest, or \$106. Under discount, one interpretation is that you sign a note for \$100 and if it is discounted at 6 per cent you would receive \$94. Then you pay back \$100 at the end of the year, and effectively, for the sake of argument, you have paid 6½ per cent.

The loophole is under a loan repayable in instalments where a \$100 note of 12 instalments of \$8.34 is signed, and instead of deducting simple interest of \$3.25 and giving the customer \$96.75, they take off \$6 from a loan repayable in instalments and he still pays back 12 times \$8.34, if it is for \$100; but instead of that being 6 per cent interest, or 6 per cent discount, it is actually 11 per cent simple interest.

Personally I feel that this is a faulty interpretation of the Act. I think the Act is properly written, and I personally feel, although I am not a lawyer, that the way the banks are counselled is faulty, and that the Treasury Board should have said that under the act they were breaking the law. This is my opinion.

I do not think it requires a good definition. You have it. It is all profit. The thing trips up on the distinction between a note payable in full at the end of the year and one paid in 12 monthly instalments. This is where the 6 per cent jumps up to 11 per cent.

The CHAIRMAN: We appear to have no further questions of Mr. Pope, and that being the case, unless members have any further detailed questions which have not been—

Mr. CLERMONT: Mr. Chairman, to support the remarks I made earlier regarding foreign banks operating branches in the United States, I refer the Committee to an article in the *National Banking Review* of September 1966 at the bottom of page 2:

Between 1961 and 1965, 15 foreign banks opened 23 branches in New York.

The CHAIRMAN: Thank you very much, Mr. Clermont.

I think we should thank Mr. Pope for giving us the opportunity of hearing some of his very stimulating views on the matters before us, particularly with respect to the operation or non-operation of foreign exchange in the international field, as it pertains to our own banking system.

I declare this meeting recessed until 3.45 p.m. at which time we will hear from Lafferty, Harwood & Company.

#### AFTERNOON SITTING

The CHAIRMAN: I think we are in a position to resume our meeting.

Our witness this afternoon is Mr. R. G. D. Lafferty of the firm of Lafferty, Harwood & Company. The firm is a member of the Montreal Stock Exchange and the Philadelphia Stock Exchange. I think this introduction will identify our witness with respect to the area in which he deals and I would invite him to submit his brief.



I did not have a chance to tell him this before we began but, of course, rather than present the brief verbatim, if it is lengthy I would ask him to attempt to summarize his major points for us, following which we will have a period of questioning and discussion, first on the points he has presented to us through his brief and finally, if time permits, any other points the members wish to raise. Mr. Lafferty, please.

Mr. R. D. G. LAFFERTY (*Lafferty, Harwood & Co.*): Thank you very much, Mr. Chairman.

Mr. Chairman and gentlemen of the Committee, we have prepared our brief in the belief that the wealth of this nation is being progressively dissipated by a banking system that exploits rather than creates. This condition results from a highly concentrated monolithic structure with interlocking interests which employs restrictive practices and prevents new initiative and enterprise from challenging the dominant position. These restrictive influences extend into industry, to interlocking interests, to cartelized trusts similar to George Weston, Argus Corporation, Power Corporation and certain large influential pension plans. The dominant position of Canadian banks in the financial community restricts the healthy growth and development of Canadian capital markets.

It is our understanding that in the United States the banks were forbidden from engaging in corporate underwritings many years ago because of the undue influence it gave the banks to those needing money and those financial institutions which are necessarily dependent on a flow of new investments. The major part of this underwriting operation in Canada takes place without competition or syndicate bidding participation. It was only open to those members of what might be termed "the financial ring". This atmosphere, in turn, breeds in the stock exchanges an environment which is more like Tammany Hall than that of a well administered free enterprise exchange market.

At the same time, the provincial governments cannot exercise their jurisdiction to properly legislate security regulations when the banks play such a major role in the community and are protected by federal legislation. As a result of this combined power, the financial press and those acting as investment research analysts cannot express an independent view, if this reflects on the system, without fear of economic reprisal. As a result, the consumer and investor is deprived of an alternate viewpoint, and through this deprivation is exploited. The management of the chartered banks in Canada have continuously failed to respect the rights of the shareholder in their financial reporting and have in many instances deliberately misrepresented the position under the guise that they were acting in the best interests of the public. The banks have assiduously maintained a protective barrier of hidden reserves in which adjustments can be made only on an annual basis and as a means to prevent the shareholders and the market place from judging the comparative competence of their management and operations. They have conducted themselves in total disregard of their fiduciary responsibilities that are inherent to their occupation. They are a law unto themselves in the marketplace, immune from the normal principles of anti-trust and anti-combine legislation.

As taxpayers we are now spending millions of dollars to educate young Canadians in a business environment where initiative, energy, enterprise and intellectual honesty are penalized because they challenge the dominant struc-

tures. It is no wonder that Canadian business "management" is so sterilized that U.S. corporations, disciplined by legislation which requires them to serve the consumer, can walk into the Canadian market and run circles around most Canadian enterprises operating on their own home ground. It is not superior technology as such; it is planning based on initiative and enterprise, qualities that have been driven out of the Canadian corporate life by the dominant interests who seek conformity and competition by the agreed division of markets.

The submission of our brief and our appearance before this Committee is based solely on a desire to contribute to a way of life that is intellectually honest and not permeated by the pervasive influence of collusion to exploit and intimidation.

Would you like us to go through the proposals we make, Mr. Chairman, or are they proof in themselves?

The CHAIRMAN: Well, they are in the brief and, as you know, the brief has been—

Mr. LAMBERT: Mr. Chairman, may I put a question? Which one of the representations are we to study, the brief that was appended to the memorandum or this completely unrelated document, it appears to me, which is now being presented by the witness?

The point is this. Usually these summaries that are presented beforehand are a summary of what is in the brief. Mr. Lafferty has made other observations which are not related and, to say the least, they are challenging and I would like to be able to go back and refer to the wording thereof, but we have not got them.

The CHAIRMAN: I think in fairness to Mr. Lafferty, it appears to me at least that what he was putting forward was a summary of the general discussion that takes up the major part of his original brief, which has been resubmitted, together with his further addendum, and I gather it led up to the specific proposals beginning on page 27 of the original brief, and also the further specific proposals in his subsequent document. Now, it is true that this method of presentation creates for me, as Chairman, some problem of suggesting to the Committee the most orderly way of considering the matter. As I say, perhaps I placed a different interpretation on Mr. Lafferty's words than you did, Mr. Lambert, but I thought he was attempting to summarize his rather detailed and closely argued discussion which took up, as I say, the first 26 pages or so of his original brief.

Mr. CLERMONT: Mr. Chairman, I read this document dated September 6, 1966 at noontime and I did not notice the same thing as that which the witness was bringing up. I noticed there was some relation but it seemed to me there was a vast difference.

Mr. LAFFERTY: Perhaps I should explain the briefs, Mr. Chairman. The original brief was presented on the first submission of the bill, which I think was Bill No. 102, and there was a date by which the submission had to be presented. We submitted our brief as of that date. Subsequently a new bill was introduced. The option was then up to us whether we wished to pull our original brief and submit a second brief, or whether we would submit a supplement to the first



brief, and the document dated September, 1966, was the supplement to the first brief. The basic theme is discussed in the original brief.

Mr. LAMBERT: That is fine. I am sorry, Mr. Chairman, but your powers of correlation must be much greater than mine, because I find a great deal of difficulty in correlating the summary that we have now heard with the closely argued purposes of the original briefs. I would like to direct the discussion, if we could, to what is before us.

The CHAIRMAN: In the brief.

Mr. LAMBERT: Yes, rather than the summary.

The CHAIRMAN: I quite agree.

Mr. LAMBERT: We have not got the summary before us.

The CHAIRMAN: I quite agree, and this has been our practice until now. I think it could be taken that the documents which we are going to discuss and on which we are going to question Mr. Lafferty are those which have been filed with us pursuant to our rules. I think, therefore, what we have to decide now is the best way to proceed, and it seems to me—and I throw this out for consideration—that we might first deal with each of the specific recommendations at the tail end of the original brief, move on from those to the specific recommendations in the addendum that has been submitted, and we can bring in any questions we may have on the general discussion as they appear to relate to each specific proposal. If that does not seem to fit, then we can keep any further questions we have as to the general discussion in the original brief, and so on, for the time that remains after we deal with the recommendations. I say this because I presume that what Mr. Lafferty is interested in doing in appearing before us as an interested and involved citizen is making specific recommendations with respect to possible legislative changes.

Now, mind you, this is a rather complex matter to attempt to divide up in some orderly fashion. If there are some other suggestions as to how to tackle this, I certainly would be happy to hear about them. Do I have any other suggestions how we might go about this?

Mr. CLERMONT: Are these two briefs the same?

The CHAIRMAN: Not completely, no.

Mr. CLERMONT: I thought when we started out that the briefs were supposed to be the same, the one that was—

The CHAIRMAN: In fairness to Mr. Lafferty, he prepared a brief with recommendations based on the original bill. I presume—although I have not asked him about this—that after considering the new bill he felt that the proposals in his original brief still applied and he resubmitted it together with some additional views which seem to apply more directly to the new bill. This has happened on several occasions in the past. I think that some of the academic witnesses who appeared before us before Christmas did the same thing.

There is a difference in numbering which we will have to deal with, but I think the best thing we can do to get right down to the discussion and questioning of Mr. Lafferty on the views he wants to put forward is to decide, perhaps arbitrarily, on some method of approach. My own suggestion to the Committee,



unless the Committee wants to do it differently, is to deal with the specific recommendations in turn, beginning with the ones that he submitted last year and moving on from there to his additional ones.

Mr. CLERMONT: Mr. Chairman, will the addition that Mr. Lafferty has supplied to his 1965 brief be a résumé?

The CHAIRMAN: I did not get that impression, Mr. Clermont. Again, in fairness to Mr. Lafferty, I think it can be said that his additional brief is related to the general philosophy put forward in his first brief. The points of specific recommendations in the addendum are with respect to points not dealt with specifically in the original brief. Have I grasped the concept correctly?

Mr. LAFFERTY: This is outlined in the first page of the second brief, explaining that this was a supplement to the first.

The CHAIRMAN: If any of the points seem to overlap in the opinion of any of the members, I would like the members to draw that to my attention. If not, as I say, in the absence of some further suggestion from the Committee, I suggest that we proceed along the lines I have outlined and invite questions firstly to the proposal on page 27, wherein it refers to section 19, which is now section 18. I think that is an orderly way to proceed. Mr. Lafferty sets out the proposal and then gives the purpose, as he sees it, behind this proposal, and I invite the members to place any questions they have on this specific proposal.

Mr. LAMBERT: Why do you make your first proposal?

Mr. LAFFERTY: There is a philosophic treatise behind this whole presentational brief. The banks have contributed to a suppression of the growth or development of free enterprise economy in Canada, and as we do have interlocking interests in Canada—you may not believe this, Mr. Lambert.

Mr. LAMBERT: I certainly disagree with you entirely there.

Mr. LAFFERTY: This is your privilege. It is equally my privilege to state otherwise.

Mr. LAMBERT: Quite right.

Mr. LAFFERTY: This is the purpose. Where you have an interlocking directorship, you have a transgression of a fiduciary capacity.

Mr. LAMBERT: Even between, say, an insurance company and a bank?

Mr. LAFFERTY: Sure you do.

Mr. LAMBERT: Or an investment dealer?

Mr. LAFFERTY: And a bank? Sure you do. Or a banker acting as a director of another corporation. He is using information available to him from his position in the bank which is derived from other customers, service and other corporate structures.

Mr. LAMBERT: Well, it is your view. That is all I can say for it.

The CHAIRMAN: Do we have further questions on this specific proposal? Mr. Laflamme?

Mr. LAFLAMME: I suggest that when you refer to the proposed Bill No. C-222 you see some proposed articles which deal with your first suggestion that there should be a restriction?

Mr. LAFFERTY: That is correct, yes.

Mr. LAFLAMME: Do you really think that the proposed legislation gives some relief?

Mr. LAFFERTY: It gives some relief but not complete relief.

Mr. LAFLAMME: What would complete relief be?

Mr. LAFFERTY: No banker nor any officer of a bank would be authorized or could accept an appointment as a director of any outside corporation, whether resident or non-resident.

The CHAIRMAN: At the moment we are dealing with financial institutions. You have another heading with regard to the other types of corporations. For the moment, let us get your views on whether or not you feel what is in the present proposed act receives your approval with respect to the eligibility of bank directors to serve on boards of other financial institutions.

Mr. LAFFERTY: I believe there should be complete separation. There is a confliction between institutions and interests from a competitive viewpoint.

Mr. LAFLAMME: You state that the proposed law does not go far enough.

Mr. LAFFERTY: It is not complete. It recognizes part of the principle. To recognize part of the principle is compromise, rather than the real principle.

Mr. LAFLAMME: In itself, what is wrong with being, let us say, a director of a bank and also being a director of a trust company, which does not in any sense control the bank?

Mr. LAFFERTY: You are accepting deposits at both banks; you are serving different customers; you are using your knowledge of one either for the advantage or disadvantage of the other. The whole theme of our submission was that we lacked competitive enterprise in Canada because we have an interlocking relationship of accommodation on the cartelization of markets, and if we were going to compete on a free enterprise basis with the United States economy and world economies we must similarly go into the same type of structures.

Mr. LAFLAMME: May I refer to page 2 of the supplement to the brief you have given us. In the last paragraph you say:

Nearly every investment dealer is dependent on a bank for financial accommodation in order to carry his bond inventory.

Is there anything wrong with this?

Mr. LAFFERTY: Not at all, as long as this is not used as a point of coercion over the investment dealer. But you can carry this a little further. Once you come to this question of the whole underwriting business and the fact that the dealer is dependent on the bank for accommodation, if he does not acquiesce or conform to the convenience of the bank, then he is subject to what I should term economic reprisals, and he has no alternative choice as long as there is an association amongst the banks and the banks are not functioning on a competitive basis.

The CHAIRMAN: Have you finished, Mr. Laflamme?

Mr. LAMBERT: As a supplementary question, is it not a fair proposition, though, that if you borrow money from a bank the bank should perhaps have the

right to supervise your operations with other people's money which they have lent to you, of if an investment dealer gets a half million dollar line of credit does he then get carte blanche to do as he sees fit? Is this the general principle of operating business?

Mr. LAFFERTY: No. If it were then, conversely, the depositor in a bank would have the right to supervise the management of those assets. A bank has a right to make a line of credit but not to supervise its use. It has a right to ask the purpose and to ensure that the agreement which was undertaken is fully worked out.

Mr. LAMBERT: But the depositor has the right to do that. If he is not satisfied with the operations of the bank he withdraws his money, the same way that a bank, if it is not satisfied with the operations of an investment dealer, it withdraws its line of credit.

Mr. LAFFERTY: Fine, as long as the bank gives a reasonably sound reason for doing so, but if it does it just for vexatious purposes—

Mr. LAMBERT: You used the term "vexatious". Those are pretty wide-sweeping terms, I think, Mr. Lafferty. I think we must have proof that this is done. You have used some rather wide-sweeping terms this afternoon, obviously in sincerity, based upon your judgment and your knowledge of financial affairs in Montreal, but we would like to see a little proof of that.

Mr. LAFFERTY: The position is this. I do not have the right to either subpoena the records of any bank, nor do I have the right to subpoena any witnesses. Mine is merely an individual's expression of viewpoint. I have been exposed to circumstances under which this takes place. A recent example took place on the west coast, where a line of credit had been granted to extend until July of next year. It was called in August when money was extremely tight. There was no reason for it being called, it was a legitimate loan, it was a natural wood industry, lumber, properly secured and the people had been in business 16 years. This was called. Now, the motives of the bank were never disclosed. This is the way this occurs. This had the effect of throwing 200 people out of employment. Now, whether there was a competitor behind the scenes who was friendly with the bank and who sought to force him out of business, I do not know, but they could not go to any other bank and get alternative accommodation. This takes place.

Mr. LAMBERT: Yes, but we have seen the restriction of credit operate time and time again when there is a general operation. There is a general operation in other sources, too. Surely to goodness an improper motive cannot be attributed to every credit restriction.

Mr. LAFFERTY: No, I do not suggest there is, but I suggest you look into the U.S. banking system. There has been a great deal of criticism of the Mercantile Bank, but they have done a great deal more up here to contribute to free enterprise and proper banking than we have ever had before. You have the Mercantile Bank and they give a line of credit and you get it in writing. Most Canadian banks will not give it in writing nor by word of mouth. They may want to change their position, and they either change the manager or they change their tune and they produce nothing in writing; whereas the Mercantile Bank will produce something in writing; a year's term loan, five years, basis of



repayment, terms, how it should be handled, their right to see the books, their right to see the operation of the company to whom the loan is being made. Then you have a document, you have an agreement between the borrower and the lender, but this is not so in most of the Canadian system.

Mr. LAMBERT: Well, Mr. Lafferty, from personal experience I can cite you an example where the bank you cite right now as a paragon of virtue in this regard pulled the rug right out from under an operation and put it into bankruptcy, entailing bankruptcies all along the line.

Mr. LAFFERTY: I am not talking about one bank or another. All I am suggesting is that the legislators should provide principles whereby I, as a citizen or consumer, has a right to an alternate choice or I am protected against this.

Mr. LAMBERT: If you read the American financial press you will see that they have a great deal of tight money down there. I have not seen any difference between the United States and Canada when it comes to that. You are saying that the independent banking system in the United States is preferable to the Canadian branch banking system because apparently it is more competitive. I think at the present time its only distinction is that it is more competitive in being tight. I disagree with Mr. Lafferty there.

The CHAIRMAN: The next name I have is Mr. Cameron, followed by Mr. McLean, Mr. Flemming and Mr. Clermont.

Right now, as I said, we are trying to keep our questioning to Mr. Lafferty's proposal that no one should be a director of a bank if he is already a director of another financial institution. Perhaps we might deal with the point as to in what areas the proposals of the present law do not meet his suggestions. Someone may want to do this at some point.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Lafferty, I think the purpose of your recommendation is to prevent or, perhaps, undo what you feel is an undue concentration of financial power at the present time. The question in my mind is would your suggestion or, as a matter of fact, the proposals in the bill before us really have this effect? Will we not be doing something legislatively and imagining that we are setting up the safeguards you speak of and really not be accomplishing something?

Mr. LAFFERTY: I think you would be contributing. I do not think you would achieve the ultimate purpose, no. This present legislation has evolved over many years. It is an adaptation of a system from the other side, but wide preventative that might help contribute to a gradual competitive environment—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Do you really think that the existence of bank directors on boards of other banking institutions is a necessary tool for exercising this monopolistic power? Would it not be done without that?

Mr. LAFFERTY: It would be more difficult.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): You think it would be more difficult?

Mr. LAFFERTY: There is no question about it. You would not have somebody else's statement of financial figures available to you which you could bargain

off to somebody else who had a *quid pro quo* in a mutual area and the advantage you wanted was somebody else's, who was a competitor of yours. It gives you bargaining power.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Then in what way do you consider the proposed amendment to the Bank Act falls short of this?

Mr. LAFFERTY: It does it completely all the way. It recognizes the principle but it does not go all the way.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It eliminates interlocking directorates in banks and trust companies and loan companies.

Mr. LAFFERTY: It reduces, I think, to a proportion of one being on the other.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes.

Mr. MORE: I wonder, Mr. Chairman, if Mr. Lafferty could use the microphone? We cannot hear him when he speaks in that direction.

Mr. LAFFERTY: I am sorry. It is my fault.

The CHAIRMAN: If you would just pull the microphone a little closer.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I think your objective is possibly quite desirable but I am just wondering whether it is practical.

Mr. LAFFERTY: There is nothing impractical about it. It is a simple stroke of the pen.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, I know, but we might be deceiving ourselves in thinking that we have a safeguard, that we have done something, and actually find that we have not.

Mr. LAFFERTY: There is no advantage to the present relationship other than it provides a channel of communication. Each should stand on their own feet and develop their own institutions and their own operations based on internal principles rather than imitating, copying or borrowing from each other or exchanging with each other. Then you have a competitive environment of initiative and ideas. You then have a creative process.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yet in other fields we find collusion, shall we say, taking place, do we not, without the existence of interlocking directorates?

Mr. LAFFERTY: This is because we do not have strong enough anti-trust and anti-combine legislation in Canada.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): We have the Combines Investigation Act, which is rather—

Mr. LAFFERTY: It is not strong enough. It did not prevent Canadian Breweries from putting all the breweries together.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): No. I do not know whether it can do so. It is very dubious, mind you, whether we are really accomplishing much by doing this.

Mr. LAFFERTY: I think it has been the principle of the United States' system that one has achieved a freedom to the consumer of avoiding this collusion and this cartelization, and therefore you provide a range of choice to the consumer.

I think if you related this to the U.S. economy you would find it has more vitality than ours. It provides a foundation for new initiative, stimulation and free enterprise, which are principles of competition by new ideas.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Those are all the questions I have now. I was just making a point, Mr. Lafferty. I am more interested in your second proposal with regard to directors of other corporations.

The CHAIRMAN: I now want to recognize Mr. McLean, followed by Mr. Flemming, Mr. Clermont and Mr. Lind.

Mr. McLEAN (*Charlotte*): You do not believe that a director of a bank should be a director of an insurance company?

Mr. LAFFERTY: No, I do not. In the brief, I think, there is one example cited where there are four bank directors sitting on an insurance board which controls a trust company, or a large position in the trust company.

Mr. McLEAN (*Charlotte*): I believe you gave us to understand that you think the banking system in the United States is preferable to ours.

Mr. LAFFERTY: Yes, I think it is.

Mr. McLEAN (*Charlotte*): Do you remember something which took place a little over 30 years ago when every bank in the United States was closed? Do you remember that?

Mr. LAFFERTY: I do not remember it but I am aware of it.

Mr. McLEAN (*Charlotte*): It is a fact, is it not?

Mr. LAFFERTY: Certainly, I am aware of it.

Mr. McLEAN (*Charlotte*): Now, they have interlocking directors in the United States in the banks?

Mr. LAFFERTY: There is legislation in this area.

Mr. McLEAN (*Charlotte*): Do they not have interlocking directors? I have read the list of directors and they say they are directors of this and directors of that.

Mr. LAFFERTY: They are directors but not of two financial institutions.

Mr. McLEAN (*Charlotte*): Well, I do not know about financial institutions. Maybe they are not directors of two banks but they certainly have interlocking directors in the United States.

Mr. LAFFERTY: Yes. You will find the president of General Motors on the board of some bank.

Mr. McLEAN (*Charlotte*): Yes. Now, you favour the Mercantile Bank coming in here?

Mr. LAFFERTY: No, I do not favour. This was not the word I used.

Mr. McLEAN (*Charlotte*): I took from the brief that you favoured something like that, foreign banks coming in here.

Mr. LAFFERTY: This comes later in the brief. I see your point there.

Mr. McLEAN (*Charlotte*): Yes, If they have interlocking directors there and the bank comes in here, it is owned in the United States.



Mr. LAFFERTY: Yes, but there are 14,000 individual banks in the United States and to interlock 14,000 is a lot more difficult than to interlock what we have here.

Mr. McLEAN (*Charlotte*): The biggest bank in the United States is interlocked as are its branches. Does it not have \$15 or \$16 billion in the Bank of America?

Mr. LAFFERTY: Yes. This is a state law of California.

Mr. McLEAN (*Charlotte*): Yes.

Mr. LAFFERTY: I do not approve of it.

Mr. McLEAN (*Charlotte*): Yes. It is the biggest bank in the United States.

Mr. LAFFERTY: I do not approve of it.

Mr. McLEAN (*Charlotte*): You do not approve of it but they have it just the same.

Mr. LAFFERTY: Yes, surely.

Mr. FLEMMING: Is your objection to one man being a director of more than one financial institution based on your opinion that this would lessen the competition as between the financial institutions themselves?

Mr. LAFFERTY: Correct.

Mr. FLEMMING: Take the case of a Mr. Jones who is a director of XYZ banking corporation. Here is his competitor and the shareholders of the competing institution. They meet and decide that they want to elect this gentleman as a director of their bank. Having done so, are they not conscious of this possibility which you express, and in their opinion would it not be an advantage to them to have him on their board in spite of your misgivings? I would like to have your comment on that.

Mr. LAFFERTY: If they are a weaker institution they would probably strengthen their position by tying the two together. If they could not compete on their own feet, then they would seek to collude, but they would be serving the consumer.

Mr. FLEMMING: I gather that your main objection is that it lessens competition?

Mr. LAFFERTY: Yes, this is correct, because if he joined the other bank or the other institution and the first institution had plans for a branch in a certain area, and then he conveyed this information to the board of the other one who wanted to maintain their position, they say, "well fine if you do that we will put another branch in the other area". Then they both decide, "well, we will compromise on this; you put one here and we will put one there". You are not moving on the correct economic principle of supply and demand and of the market place.

Mr. FLEMMING: I take it that you are afraid there would be a degree almost of collusion and it would be to the disadvantage of the general public to do otherwise?

Mr. LAFFERTY: Of the consumer. You are standardizing the services.

Mr. FLEMMING: Speaking about the American system, for instance, which is a multiplicity of small banks rather than our system of larger banks, is it not true that in many instances they own their trust companies holus-holus?

Mr. LAFFERTY: No, I do not think so. I think that in the majority of the states the banks can undertake trust activities which we cannot do up here.

Mr. FLEMMING: Do they have federal regulations governing their activities in this respect or is it entirely state, or is it both?

Mr. LAFFERTY: No, banks can function in the capacity of trust accounts.

The CHAIRMAN: It was my understanding, Mr. Flemming, that there are no regulations in the United States specifically banning the interlocking directorates of financial institutions even to the extent that the government is proposing in this bill. What is your comment on that, Mr. Lafferty?

Mr. LAFFERTY: I understand there is, Mr. Chairman. It may vary from one state to another. I looked it up when we prepared the original brief and found a reference on how it was established, but surely someone from the Department of Finance could check that.

Mr. FLEMMING: I can see an objection to a man being a director of a bank and being a director of other business activities. I think I could follow that all right, but I fail to see—certainly to the same extent that you do, Mr. Lafferty,—the great objection to the same man being a director of two banks.

Mr. LAFFERTY: Because then they decide to work in one direction together to achieve certain results.

The CHAIRMAN: Of course, we should remember that the proposed legislation which we are really considering would prevent interlocking directorates of banks and trust companies, and also with respect to banks and other companies beyond a certain proportion. I gather, Mr. Lafferty, that you propose this be extended to any financial institution, as you define it in your brief?

Mr. LAFFERTY: I defined the financial institutions, yes.

(Translation)

Mr. CLERMONT: Mr. Chairman, I refer to page 27 of the brief, and I quote:

(English)

“In banking and finance two masters cannot be reliably served at the same time. There are conflicting interests involved. The shareholder has the right of undivided interest from the directors of his bank”.

(Translation)

Although I read in reference to Bill C-222, Section 19, that the directors are elected by the shareholders at the annual general meeting. Would you make comments in that regard? If shareholders have the right to choose their directors—

(English)

Is the translation not coming through, Mr. Chairman?

Mr. LAFFERTY: I had the wrong plug on, pardon me.

Mr. CLERMONT: Mr. Lafferty, according to page 27 of your brief the shareholders should have the right to choose their directors.

Mr. LAFFERTY: In principle.

Mr. CLERMONT: Do they have that right?

Mr. LAFFERTY: Yes.

Mr. CLERMONT: And they know if they nominate and appoint so and so that he might be president of Alcan or the CPR or another finance company?

Mr. LAFFERTY: Yes, they have the right; but, in practice, they do not have the means of judgment, firstly, because the reports which are presented to them are not complete and do not state accurately what the bank's affairs have been during the past year; therefore, they cannot make any judgment about the management itself. Secondly, they are not usually given any prior background on the new director, on the man you are now proposing as a nominee for the board for the next year. In principle, they have the right to dissent, but in practice they have very little power.

Mr. CLERMONT: Yesterday, or the day before, I referred to the annual report of the Bank of Montreal. I looked at the list of directors. I doubt very much if many of the shareholders will not know the gentlemen who were nominated.

Mr. LAFFERTY: They will know them by name and they will see their pictures in the papers I guess, yes. They do not know about their business interests, or what their background is.

Mr. CLERMONT: They might not know all their connections, but they will know some of them because these are people known in financial circles and in industry.

Mr. LAFFERTY: They are known figures in financial circles, but the financial circles are not all the shareholders.

Mr. CLERMONT: Mr. Chairman, at page 1 of his brief, Mr. Lafferty, or whoever prepared it, says:

For many years the view has been publicly expressed by Canadian bankers and other prominent persons that Canada has the finest banking system in the world. We suggest that, before the Committee accepts this view, they obtain the opinion of authoritative people in the Federal Reserve System of the United States and other prominent bankers—  
and so on. According to this brief the American banking system is the best in the western world, although this morning another witness claimed that the English banking system was the best in the world.

Mr. LAFFERTY: Then you have a division of viewpoints.

Mr. CLERMONT: Have you any information to give to this Committee concerning these remarks?

Mr. LAFFERTY: The thought here, Mr. Clermont, was that, before the Committee, or the legislators, made any judgment, perhaps the whole, over-all legislation would come into better perspective if they familiarized themselves with the U.S. system. The contention was supported that the U.S. system tended to have a more efficient operation, because if you look at the productivity of the



United States in relation to its gross national product and other matters you find it is a more efficient economy than the Canadian economy. Now, there must be some basic reasoning on why that is.

Mr. CLERMONT: But do you not think that our Canadian banking system has some merit, too? One of our Canadian banks, I understand, is the fourth largest in North America, and one or two more are within the twenty-five biggest in North America.

Mr. LAFFERTY: It is a misconception that size is necessarily efficiency. The largest size of government is not necessarily the most efficient government.

Mr. CLERMONT: That is your opinion.

Mr. LAFFERTY: This is my opinion.

The CHAIRMAN: Do you not think, Mr. Lafferty, that asking the opinion of United States bankers and members of the federal reserve system is what is known in legal circles as self-serving evidence?

Mr. LAFFERTY: It may well be called that, if you ask me, but I do not know. I think that you would be broadening the understanding of what the differences between the two systems were, and what the merits of the various aspects were.

*(Translation)*

The CHAIRMAN: Any other questions, Mr. Clermont, in this regard?

*(English)*

Mr. CLERMONT: No, Mr. Chairman.

The CHAIRMAN: Mr. Lind?

Mr. LIND: What I would like to say regarding the interlocking directorates has reference to the statement at the bottom of page 2 which says:

The one exception is that the service accorded to a customer is graduated, depending on his importance to the bank in the over-all scheme of things. Friends of the bank, that is to say friends of the hierarchy, receive special accommodation, special rates and special favours.

What proof have you that this practice exists? I would assume that you are referring here to directors receiving special accommodation from banks, and special rates.

Mr. LAFFERTY: I have no proof. As I said before, I have no right to subpoena either witnesses or evidence. I think those who live in the financial community are reasonably aware that this is so.

The CHAIRMAN: On what do you base your comment? Did you just dream it one night?

Mr. LAFFERTY: No; as I say, those who live in the financial community are aware of these things.

The CHAIRMAN: Could you tell us a little more about this? It would be very useful to us to have more information on the basis.

Mr. LAFFERTY: Well, I mentioned in my original, opening notes these large, cartelized trusts, such as Argus Corporation, and other companies. These do not

come out of the normal scheme of things. This is through the assistance of various banking institutions. I do not know whether you gentlemen have ever looked at the balance sheet or annual statement of Argus Corporation, at the extent to which it dominates Canadian corporate life and industry, and the extent of the equity capital and how small it is, and how much of Canadian savings are in the debt, and the basis of capitalization for the benefit of those who operate the corporation. I do not know how far you have gone in this legislation; but this has been a major factor in the corporate and financial life of this country.

The CHAIRMAN: But, Mr. Lafferty, you are leaving inferences of malfeasance, or evil intent, or evil conduct, in your brief. Perhaps I have drawn that inference and it may be that others have, as well. I think that it would be very useful for the Committee to have some indication of the basis on which you make this type of comment.

Mr. LAFFERTY: All I can relate it to, Mr. Chairman, is that these are views that I hold after some exposure to the financial community. I am not in a position that I can undertake to prosecute my views. I have not the staff to do it, nor have I the right, or the access, or the authority to get the information I would need to do so. I would not express the views without some conviction or belief that it took place. You may not believe my views; that is your choice.

The CHAIRMAN: Well, I am not saying whether I believe them or not at this point.

Mr. LAFFERTY: It is your function to investigate whether they have validity, or not, using the powers and the authority that you have to do so.

The CHAIRMAN: But, look here, it is a basic principle of Canadian justice that he who asserts must prove; that is how you start off—

Mr. LAFFERTY: I have expressed a viewpoint; I cannot prove it without, as I say, having access to the books and calling witnesses.

The CHAIRMAN: But what concerns me is that I gather from your brief that you are doing more than expressing views. You are stating things as facts and I got the impression, from a study of your brief, that when you did appear here you would be able to back them up with facts and figures. I was looking forward to the opportunity of getting the facts behind these assertions which I took to be more than expressions of opinion, but as statements which could be supported.

Mr. LAFFERTY: No; they are based, I think, on a reasonable knowledge of what takes place.

The CHAIRMAN: Well, give us the benefit of this knowledge.

Mr. LAFFERTY: I cannot do this without implicating people. I do not have the right to implicate them. The whole theme of the brief is that the system creates these conditions—that is, the nature of the legislation.

The CHAIRMAN: Well, of course, this brief is presented to us as part of our proceedings, and it is available to be read by all sorts of people. I think those who are interested in the subject should have the benefit of knowing on what you base these statements.

Mr. LAFFERTY: I have just explained it to the extent that I can.

Mr. LIND: Mr. Chairman, may I continue with my questioning?

The CHAIRMAN: Yes.

Mr. LIND: In your statement you say that customers are graded, depending on their importance to the bank in the over-all scheme of things. Are you saying that there are different levels of loans, or loans made to certain people at various beneficial interest rates?

Mr. LAFFERTY: Sure.

Mr. LIND: From perhaps,  $4\frac{1}{2}$ , as we heard about this morning—which was quite an eye-opener—up to 6 per cent?

Mr. LAFFERTY: The more important a customer is, or the more influence he may have with the bank, the more favoured treatment he is likely to receive.

Mr. LIND: I understand that you are in the bond business; is that right?

Mr. LAFFERTY: No, I am not; I am a financial analyst.

Mr. LIND: Without giving names, can you point out to us any of these—various rates of interest and where they would apply? Is there an over-all position where, say, taking it in the broad sense, the government of Canada would borrow at the cheapest rate, the province of Ontario may be the second, or the province of Quebec, or *vice-versa*, then a municipality, and then an institution like Argus Corporation—which you mentioned has a very preferential rate—and could you give us the various rates.

Is this due to interlocking directorates? This is what I am going to try to tie down.

Mr. LAFFERTY: I do not know whether this would perhaps explain it any more clearly. I, in my original notes, introduced this question of underwriting. Underwriting, as you know, is the financing of capital for a corporation.

Take one of the major corporations, such as Bell Telephone. Its underwriting is not on a competitive bases. One of the major banks, with one of the major dealers, agrees with the company what price the company will pay for the money. This is not on a competitive syndicate or competitive-bidding basis. In this particular issue the original price paid to the chartered bank, or the banking member, was \$98; it went to the banking group member at a price of \$98.25; then it went from that group to the selling group members at \$98.65; it went to the casual dealers and sub-agents at \$99.15. it went to retail and exempt institutions at \$99.40. The total cost to the corporation was \$1.40.

A similar underwriting of A.T. & T. in the United States on August 1;  $5\frac{5}{8}$ ; \$250 million; the underwriting discount was 78 cents.

Mr. LIND: How much?

Mr. LAFFERTY: It was 78 cents.

Mr. LIND: Seventy-eight cents, and this was \$1.40.

Mr. LAFFERTY: In this particular thing there was no syndicate bidding; there was no competition; it was an agreed division. All I am suggesting is that life would be much healthier in the financial market if these were, in principle, on a competitive basis. This is dealing with principles rather than dealing in other people's affairs and things of this nature, which certainly is not in my area.



Mr. MORE (*Regina City*): You say this is because there are interlocking directors between Bell Telephone and the bank?

Mr. LAFFERTY: Well, obviously; why does the Bell Telephone go to any one group? Why do they not say, "fine; we will accept syndicates from every group. Come in, form a syndicate and make a bid. We want \$30 million cash. Come in and bid in the marketplace, and what you can find, invest in it, or find where you can place those bonds."

The CHAIRMAN: Are the interlocking directorates in this case between Bell Telephone, their banking connection and the underwriter?

Mr. LAFFERTY: Yes; but not to the underwriter. The underwriter is an affiliate underwriting the bank concerned.

The CHAIRMAN: What did you say? The underwriter is what?

Mr. LAFFERTY: Is the affiliate underwriter of the bank concerned.

The CHAIRMAN: What do you mean by "affiliate"?

Mr. LAFFERTY: If you leaf through the brief you will find that the three Canadian banks which control 70 per cent of the assets dovetail into the three major trust companies. There are also three major underwriters who interrelate to the trust companies and the branch.

The CHAIRMAN: The branch interrelates? You mean they have interrelated directors.

Mr. LAFFERTY: No; they have business relationships.

The CHAIRMAN: Business relationships?

Mr. LAFFERTY: They normally are centred in the same buildings, and they normally work as partners in their financial activities.

Mr. MORE (*Regina City*): What is the extent of the interlocking directorship between Bell and the bank concerned? You must have studied it to make the assertion.

Mr. LAFFERTY: To a sufficient extent, sir.

The CHAIRMAN: Actually this is a separate proposal, and to permit orderly consideration of this matter I think we should, at the moment, stick to the proposal to ban interlocking directorates of financial institutions, in which I think we can include underwriters to some extent. However, if we are going to talk about banks and other types of business enterprises I think we should go on to the specific proposal in that connection.

Do you have a further question, Mr. More? I am sorry, Mr. Lind. Perhaps you were not finished.

Mr. LIND: This is perhaps a further question that Mr. Lafferty has brought up, dealing with the three banks which control 70 per cent of the assets of our banking system. He makes this statement on page 3.

Is this due to interlocking directorates, too?

Mr. LAFFERTY: I would say it has, over the years, resulted from this, yes. The accumulations have resulted from this type of interlocking relationship, yes.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Interlocking directorates with what type of enterprise other than banks?

Mr. LAFFERTY: Corporate enterprises.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes; I mean manufacturing; not necessarily other financial institutions.

Mr. LAFFERTY: Oh, no; manufacturing, transportation.

Mr. LIND: Then how much do you consider that our monetary system is controlled by the whole banking system, the chartered banks—the eight chartered banks, now the ten chartered banks?

Mr. LAFFERTY: The monetary system is controlled by the central banking system.

Mr. LIND: Yes, I realize that.

An hon. MEMBER: You mean the total deposits?

Mr. LIND: The total deposits in the ten chartered banks.

Mr. LAFFERTY: I am sorry; I do not follow the reasoning behind that.

Mr. LIND: To control our monetary system, or the total, you would have to control deposits.

Mr. LAFFERTY: Deposits would be in one bank or the other, would they not?

Mr. LIND: Not necessarily; they could be in trust companies, loan companies, *caisse populaires* or credit unions.

Mr. LAFFERTY: Yes; but in most cases that would flow back into the banking system.

Mr. LIND: Is it your opinion that, due to these interlocking directorates, they control more than 70 per cent of the monetary system.

Mr. LAFFERTY: This is a contribution that has occurred over a period of many years. Their contribution as directors of various corporations has enabled these particular three banks to establish the strong position they have.

Mr. LIND: You are just referring to the three banks versus the other five banks; they control the 70 per cent of the deposits within the banking system. I am referring here to the third paragraph on page three of your brief where you say that three Canadian chartered banks control 70 per cent of the assets of the Canadian chartered banking system.

Mr. LAFFERTY: That is a factual statement.

The CHAIRMAN: We have had this information before.

Mr. LIND: How much do these three chartered banks control of the total assets of our banking system, including the near-banks and loan companies. Have you any idea on that?

Mr. LAFFERTY: Of the combined assets of the entire banking system—that is, the chartered banking system—they control 70 per cent.

The CHAIRMAN: I think that earlier it was suggested that if you take the other financial institutions, the trust and loan companies, the *caisse populaires* and so on, it comes down to 50 per cent; if you include general pension funds,

life insurance companies, general insurance companies and so on, the banks have alleged that they get down to 23 per cent. We may want to look into that again further.

Do you have further questions, Mr. Lind? Are there any further questions on proposal number one?

Mr. GILBERT: Mr. Lafferty, your restriction is with regard to directors of other financial institutions. If you look at the composition of directors of banks today, you would find that they are mostly representatives of business. It has been suggested to the Committee that there be government-appointment of directors from other groups, such as the trade unions, co-operatives and consumer associations, to make it more representative. What do you think of that idea.

Mr. LAFFERTY: I think it is accepted in principle that the bank, or whatever the enterprise is, is owned by the shareholders. In principle, they have the right to elect whomever they wish as directors. The Government has no right to intervene in the operation of the enterprise. I suppose what you mean is legislation so that the others can make representations to the shareholders by suggesting what could be done for those banks, or what could be done for those shareholders; but it is beyond the prerogative of the government to intervene directly and place or appoint its own directors on these institutions.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Has the government ever done this since we have had the Bank Act?

Mr. LAFFERTY: Not to my knowledge.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): They have intervened in the operations of the banking business.

Mr. LAFFERTY: They have intervened in the regulation of the banks, but this is governed by the legislation which you people pass.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Is there not also a certain amount of intervention, or possible intervention by the Inspector General with regard to the categories of loans.

Mr. LAFFERTY: Sure; I think this is just within the—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): There is government intervention in the operation.

Mr. LAFFERTY: There is government influence, yes. There is government influence right through our lives.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, but intervention, I said.

Mr. LAFFERTY: All right, government intervention. I do not think the Inspector General could actually stipulate whether or not a bank should increase its position in one industry or decrease its position in another, unless he has legislation to back him up. Whether he has any authority, I do not know. I do not think he has, within the Bank Act. He might make no misuse, or his persuasion might be sufficient, but would the banks comply?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): We have had evidence that he does something more than just make his position known. He calls the bank's attention to any imbalance.



Mr. LAFFERTY: But I do not think he has the authority to do that under the Bank Act, has he?

The CHAIRMAN: I think that probably arises out of his responsibility to prevent the banks from going into a position of insolvency.

Mr. ADDISON: The point of this is that if the large trade unions take positions as large shareholders of Canadian banks then certainly they will be entitled to representation on the board, if they can hold enough shares.

Mr. LAFFERTY: Would you not say that the other shareholders should vote them into that position?

Mr. ADDISON: That is right. But they have a legitimate avenue to have people on the board.

Mr. GILBERT: Is the composition of the present boards of directors of banks representative of the shareholders?

Mr. LAFFERTY: No, not in terms of majority.

The CHAIRMAN: Perhaps we could move on to Mr. Lafferty's second proposal, a very interesting one, also on page 27.

Do you have any questions or comments on that one?

No shareholder shall serve as a director if he is also a member of the House of Commons or the Senate in Ottawa, or an elected member of a Provincial legislature.

Mr. Lafferty goes on, under the heading "Purpose," to explain why he makes this proposal.

Mr. CLERMONT: This does not concern Mr. Lafferty at all, but I will take the occasion to mention that I understand that a Mr. Gaston Clermont was, or is, a director of the National Bank. If that is the case, it is not Mr. Gaston Clermont, member for Labelle.

The CHAIRMAN: Because of your knowledgeable questions it would not have seemed—

Mr. CLERMONT: I think this is the proper place in this brief to mention it, because I have been asked: "Are you a director of a bank?" I would have been very surprised to find out that I was a director!

The CHAIRMAN: So you want to place this on the record.

Mr. CLERMONT: Yes; then the record is straight.

The CHAIRMAN: Any further questions on this second proposal.

Mr. LAMBERT: Why would you disable, or disqualify, a member of a provincial legislature, since provincial governments have no control over a federal bank? Why disqualify a member of a legislature, who is not a cabinet minister—on even if he is—who has no control over them? I can see it, if you are a member of the cabinet of the government of Canada, but why should a member of parliament be a second class citizen in his investments.

Mr. LAFFERTY: It is not a question of being a second class citizen in his investments. It is just a question of whether you should have a politically influenced leader in that institution—whether it is desirable or not for the remainder of the shareholders.

Mr. LAMBERT: Would this disentitle him to be a director of a major commercial organization that has, shall we say, a very wide influence in the country?

Mr. LAFFERTY: Yes: in one case you are, as an elected representative, serving a constituency and the people you are elected to represent. When you are acting as a director of a bank you are no longer serving those specific interests, and I would say that there would probably be a conflict is what your interests were.

Mr. LAMBERT: But would there be any greater conflict than if a member of parliament were a director of Imperial Oil?

Mr. LAFFERTY: I think it would be undesirable. I do not think a member of parliament should be connected with any Canadian corporation

Mr. LAMBERT: Even his own business?

Mr. LAFFERTY: A private corporation is fine.

Mr. LAMBERT: He may be the controlling officer of a public corporation that he organized himself. Do you think this is wrong?

Mr. LAFFERTY: Yes, I do.

Mr. LAMBERT: Oh, Mr. Lafferty; no matter what the times?

Mr. LAFFERTY: I am known as a purist in this business, and I think it is better to keep things in their areas.

Mr. LAMBERT: You mean that you would accept the concept that a person could be a director of a private corporation with assets of a billion dollars, but could not be a director of a public corporation with assets of fifty thousand dollars.

Mr. LAFFERTY: I do not think that is a realistic question because other than General Motors I do not think that we have private corporations in Canada with assets of a billion dollars.

Mr. LAMBERT: I know; but you have already told us that you are dealing with this in principle.

Mr. LAFFERTY: Yes, in principle. Now the question arises whether a private corporation when it reaches a certain size where it has an influence on the economy, should be a public corporation and exposed to public examination and public scrutiny.

Mr. LAMBERT: I think that is another very valid point.

Mr. LAFFERTY: But if it is a small private corporation, within the constituency of an elected member, and he happens to move from his business position and decide to run on a political platform, and is elected, I do not think we have reached the stage yet where he should have to divest himself completely of all his financial interests.

The CHAIRMAN: Of course, it is one of our rules now that where legislation applies specifically to something a member is interested in, other than of general application to the community at large, he must declare his interest and not vote.

Mr. LAFFERTY: I think that is sound.

The CHAIRMAN: Are there any further questions on this proposal?

I am wondering to what extent—this was also suggested by Mr. Lambert—you think a private member—and I stress “private”—of the House of Commons is really in a position to misuse his position if he happened to be a member of the board of directors of a chartered bank.

Mr. LAFFERTY: He is in a position to obtain information, either directly or indirectly, which I think is an abuse of his position.

The CHAIRMAN: What type of information are you referring to?

Mr. LAFFERTY: Either intended government policy, intended legislation, or from various government departments, through his position of influence within the legislature itself.

The CHAIRMAN: You seem to place the position of a private member of parliament above that—

Mr. LAMBERT: You are suggesting a lot more than a government back-bencher—

Mr. LAFLAMME: You are over-stating the power of the back-bencher.

The CHAIRMAN: If there are no further questions on this interesting proposal, let us go on to the next one at the top of page 28.

I will read it:

No officer of a Canadian Chartered Bank shall serve as a director of any corporation, whether resident or non-resident in Canada, so long as he is an officer of the bank.

Any questions on this proposal?

Mr. LAMBERT: Do you mean that an officer of a Canadian chartered bank could not be a director of a corporation such as RoyNat, as it now exists?

Mr. LAFFERTY: Perhaps you would turn to page 6 of the brief where we outline the directorates that an officer of one bank holds. It is my contention that if he is serving the bank and is paid a salary by the shareholders his function should be to look after their interests. It is my contention that he cannot apply himself to the interests to these shareholders if he is involved in so many other affairs.

The CHAIRMAN: Mr. Lafferty, on pages 6 and 7 you list business firms such as The Ogilvie Flour Mills Co. Ltd., Canadian Pacific Railway Co., but then you go on and you refer to such institutions as the Montreal Boys' Association; the Seignior Club Community Association Ltd.; the Canadian Council, International Chamber of Commerce; the Canada Council; the National Industrial Conference Board; The Royal Empire Society; Canadian General Council, The Boy Scouts of Canada; Member of Metropolitan Board of Directors Y.M.C.A. (Montreal); Canadian Cancer Society; Rehabilitation Institute of Montreal; The Red Cross Society; Health League of Canada; and so on.

Are you suggesting that an officer of a chartered bank should not be able to undertake service in charitable or community organizations?

Mr. LAFFERTY: No, I am not; I am suggesting that it should be related to Boards of Directors.



The CHAIRMAN: But you have listed all these.

Mr. LAFFERTY: Merely to show the range of activities.

The CHAIRMAN: You are not suggesting that there is anything wrong with an officer of a chartered bank serving on the board of the boy scouts, are you?

Mr. LAFFERTY: No, I am not, Mr. Gray; but I suggest that he cannot really do a reasonable job on all these activities. In the context of this particular area I think it talks in terms of the pursuit of power rather than the—

The CHAIRMAN: Are you suggesting that to be a member of the board of the boy scouts is to help create a power structure in Canada?

Mr. LAFFERTY: No; I will put it this way, that my complaint is that if the president of this particular bank had attended to the affairs of the bank itself and had divorced himself from his other interests, then they would not have had to call in a U.S. management consulting firm to tell them how to run their bank. They have had one of the largest U.S. managing firms in that bank for 2 years telling them how to reorganize it.

Mr. LAMBERT: Well, Mr. Chairman, if you are the chief executive officer of one company, and that is all, you can still call in a management consultant firm to get an outside view, so that you get away from, shall we say, inbreeding, or inward thinking. I fail to see the relationship of your thinking here, Mr. Lafferty. Thank God we have got people who are prepared to serve the community and their church.

Mr. MORE (*Regina City*): Do the people who take advantage of your services to look after their companies also engage in community work. Is that why you exist?

Mr. LAFFERTY: I do not understand.

An hon. MEMBER: Could you say that again a little slower.

Mr. MORE (*Regina City*): Do people that take advantage of your services in your firm—

Mr. LAFFERTY: They take advantage of our service for a purpose, and if not, they do not take advantage of it.

Mr. MORE (*Regina City*): Would not the same hold true of the bank having a consulting service come in?

Mr. LAFFERTY: This is true; but my own view is that if you are running your own internal operation correctly, it is not necessary to have them in to reorganize your structures. Presumably this is the function of management for the shareholders.

The CHAIRMAN: With respect to community organizations, including those organized in corporate form, which is quite common—I gather all those that I have just referred to are organized in corporate form—is not the matter of decision of the board of the directors and the shareholders whether it is appropriate for an officer or an official of a bank to be on these boards?

Mr. LAFFERTY: I doubt that it goes to the decision of the board or of the shareholders.

Mr. McLEAN (*Charlotte*): Mr. Chairman, I think, in this respect, they get a high officer of the bank because they are looking for contributions for the boy scouts.

An hon. MEMBER: Yes.

Mr. LAMBERT: I do not agree at all. It so happens that some men who occupy senior positions—I would say a good proportion—have not a lively and intelligent interest in the particular movements; in the same way that many leading members in the business community of the city are the most active men on boards of benevolent and charitable organizations because they like to do that kind of work. It is not because somebody thinks they have an easy, open wallet.

The CHAIRMAN: In other words, Mr. Lafferty, you are not suggesting that an official of a bank has any less responsibility to the community than an official of, say, a retail store?

Mr. LAFFERTY: Oh, no.

Mr. MORE (*Regina City*): Mr. Chairman, I think his whole case has been weakened. I think the reason that he put all these in was to make a full page, which would rather astound us. The purpose of it is obvious. He wanted to sell a point. I think it is ridiculous to list some of these and to argue the point of view that he is putting forward.

The CHAIRMAN: The next proposal is with regard to proxies. Are there any questions on that one?

An hon. MEMBER: Mr. Chairman, we have not finished with this.

The CHAIRMAN: Oh, I am sorry; I thought—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): First of all, I happen to agree with your suggestion that we should not have bank directors, or bank officers, on the boards of other corporations. What I am interested in finding out, Mr. Lafferty, is if your objection to it is the one you have just stated, that they cannot do two jobs, and that they are, in fact, moonlighting on the bank shareholders if they do this other job. Is that your objection, or is it that their joint position would enable them to secure preferred treatment for the other corporations of which they are directors?

Mr. LAFFERTY: I think it is a combination of the two. I think that the two are both equally applicable.

The CHAIRMAN: I think, in fairness to Mr. Lafferty, we should separate the concept you have just put forward, Mr. Cameron, with reference to commercial and business organizations, from—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Oh, yes; although on the point that Mr. More raised just now, I would point out there has been a growing criticism of the influence of important members of the business community on the curricula of universities, for instance; that they have an undue influence on our educational system due to their position on the boards of governors and senates of universities. I think, for that reason—and the boy scouts may come into this—that this type of non commercial appointment may be equally objectionable.

Mr. LAFFERTY: It is brought up in this brief that it restricts certain philosophies.

Mr. LAMBERT: You are not suggesting that they are intellectually senile—

Mr. LAFFERTY: No; indeed, they are not; but they divert these institutions to their own point of view.

The CHAIRMAN: Would you suggest, Mr. Cameron, that representatives of other interest groups be forbidden to sit on university boards?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I am not suggesting that they should be forbidden to sit on them, but I am suggesting that Mr. Lafferty has a point which brings in some of these other non-commercial types of appointments such as bank directors—because we are dealing with banks now—and because of the banks' key position in the economy. I think there may be some validity in that point of view.

Mr. ADDISON: Would you say that a trade union official would fall into the same category?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I would frankly view with a certain amount of doubt a trade union official's being on the board of governors of a university. I think it would give a certain limited point of view to an institution that should not have a limited, special-interest point of view.

Mr. ADDISON: Thank you.

The CHAIRMAN: I think we are on the verge of straying a bit far afield. I think we should stick to the specific point. It can be seen why Mr. Lafferty puts forward this argument that an officer of a Canadian chartered bank should not serve as a director of any corporation.

Mr. CLERMONT: Mr. Chairman, I do not think we are out of our field when someone—Mr. Lafferty, or the people who prepared the brief—says, at the bottom of page 10:

As a result, it means that the learning institutions of Canada are required to teach at a level of mediocrity in business administration, finance and economic affairs.

I do not think we are out of this field.

The CHAIRMAN: No; I am just referring to allusions to representatives of other interest groups. We could get into a very useful discussion in that area, but—

Mr. CLERMONT: This is a very strong statement, Mr. Chairman.

The CHAIRMAN: Yes; that is right. I am not saying that is out of order. I am referring to the point, on which we seemed to be about to enter into discussion, of the usefulness of having representatives of all sorts of economic interest groups on university boards.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I would suggest, Mr. Chairman, that you should not have allowed Mr. Addison to ask a question of another member of the Committee.

The CHAIRMAN: I know; but these exchanges are always very stimulating. I take the blame.

If Mr. Cameron has finished his questions I would be willing to recognize you, Mr. Clermont.



Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I just wanted to make it clear that there are the two aspects that you have in mind?

Mr. LAFFERTY: Correct.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would you extend your prohibition to bank directors, or are you confining it entirely to executive officers?

Mr. LAFFERTY: Executive officers.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Just executive officers; you do not have the same objection to an ordinary director of the bank?

Mr. LAFFERTY: No.

The CHAIRMAN: Mr. Clermont, you were referring to page 10.

Mr. CLERMONT: Yes; page 10 or page 8. According to what you say at the bottom of page 8, small companies are swallowed up by the action of the banks, and our learning institutions are not teaching the proper business administration because they are afraid of losing their endowments. Is this only your personal impression, or have you proof of—

Mr. LAFFERTY: Perhaps I should read those two paragraphs:

It means that a system is created that is wide open to abuse and exploitation by a few strong individuals. By forming small cliques serving on different bank boards, those at the apex of the pyramids are in a position to acquire and exchange information that would not otherwise be available. This is the nucleus of men who dominate the Canadian capital markets, and who by the creation of investment trusts are further able to exercise their power throughout Canadian corporate life. There are many historical examples of good medium and small companies that had real growth prospects which have been swallowed up. They had no alternative because they had no protection from price cartelization. Good and growing management must then surrender to the dictates of larger interests or be lost. Industry becomes concentrated, immobile and resistant to technological and marketing changes. The consumer ultimately suffers and more efficient U.S. industry invades the Canadian market place, and a serious imbalance in our trade figures result.

Mr. CLERMONT: I have read your brief, Mr. Lafferty, but—

Mr. LAFFERTY: In this particular case there is public evidence to refute it. If you want me to take you over the history of the Argus corporation, you will find it. It is all there. The brewing industry in that particular—

Mr. CLERMONT: I hope it is better than the 3 letters you have attached to your second brief one signed "Treasurer, A National Canadian Corporation", and the other two, without a name, just signed "A Lawyer". I hope it is better proof than those three letters.

Mr. McLEAN (*Charlotte*): Mr. Chairman, I notice that Mr. Lafferty has mentioned the Canadian brewery several times, and I do not think they are very successful.

Mr. LAFFERTY: No; but ultimately it leads to a bad and delinquent industry; there is no question; all concentration of industry does, because it lacks a competitive market. Cartelization leads to inefficiencies. That is why we are major consumers—

Mr. McLEAN (*Charlotte*): You would say that could be applied to the fishing industry, too, I suppose?

Mr. LAFFERTY: Even sardines swim in schools.

The CHAIRMAN: Mr. Clermont, do you have further questions or comments on the reference to educational institutions?

Mr. CLERMONT: No, Mr. Chairman.

The CHAIRMAN: Mr. More?

Mr. MORE (*Regina City*): Not at the moment.

The CHAIRMAN: Perhaps I can quickly ask a question about this. I am referring, Mr. Lafferty, to page 10—and I thank Mr. Clermont for again bringing it to our attention—referring to this concentration:

As a result, it means that the learning institutions of Canada are required to teach at a level of mediocrity in business administration, finance and economic affairs.

Could you give us some specific examples in these disciplines of somebody requiring an educational institution to teach at a lower level than some other institution, let us say, in another country?

Mr. LAFFERTY: I would suggest that if you had a faculty in one of the university which taught the principles of free enterprise he would ultimately find life very difficult there.

The CHAIRMAN: No. You have made a suggestion now, but in your brief you have made a flat statement.

Mr. LAFFERTY:

As a result, it means that the learning institutions of Canada are required to teach at a level of mediocrity in business administration, finance and economic affairs.

A very large number of Canadians who require an economic understanding and background go to either Harvard, or a school in Chicago, or one of the other schools in Boston. The only present business administration school I think we have, which has achieved any standing in the market place, is Western in London.

The CHAIRMAN: Now, is this not part of the ordinary ebb and flow of learning for people who go to other institutions, and countries to study?

Mr. LAFFERTY: No.

The CHAIRMAN: If somebody goes from Harvard to the London School of Economics does that mean that Harvard is mediocre?

Mr. LAFFERTY: It would suggest, if there was a trend in that direction, that one was accepted as having a teaching staff inferior to the other. We are exposed to students who come out of local universities in Montreal, and their knowledge of the market place when they come out is a pretty low denominator.

The CHAIRMAN: Let me return now. You have made a flat statement:

—it means that the learning institutions of Canada are required to teach at a level—

Required by whom, first of all?

Mr. LAFFERTY: If you had members of a faculty who taught—

The CHAIRMAN: No, no; excuse me, sir. You have made a flat statement:

—it means that the learning institutions of Canada are required to teach at a level of mediocrity—

Required by whom?

Mr. LAFFERTY: By the whole context of the overall structure of the dominant interest.

The CHAIRMAN: Give some names.

Mr. LAFFERTY: Which end?

The CHAIRMAN: Who is giving the orders?

Mr. LAFFERTY: We have the bank as the dominant interest in the scheme, which you may accept or may not accept. You may have the major banks represented on these boards of governors of these universities. If I happened to be a faculty member and I taught that the banking system was a dominant system in the faculty, I do not think that I would hold my employment very long.

The CHAIRMAN: Can you give me some evidence of this? Do you have anything that has been written—a written directive? Can you show us a written directive?

Mr. LAFFERTY: No.

The CHAIRMAN: You cannot. Can you direct us to a professor who will be willing; or able, to come to us and testify, that he is required to teach such-and-such in these fields?

Mr. LAFFERTY: I think if you went and looked you would find one.

The CHAIRMAN: No. Can you help us?

Mr. LAFFERTY: I do not have the powers to do this.

The CHAIRMAN: Then, on what do you base this statement?

Mr. LAFFERTY: This is a viewpoint, expressed, within the context of the whole thing.

The CHAIRMAN: This is only a viewpoint. I see.

How do you explain the fact that a number of the academics who have testified before us have been quite critical of the banking system?

Mr. LAFFERTY: I did not see their evidence.

The CHAIRMAN: You did not see their evidence. As far as I am aware they are still working.

Mr. LAFFERTY: May I say that up to the present time all we have received by mail are the transcripts up to number 28.



The CHAIRMAN: Well, I would take that up with the Printing Bureau.

Mr. LAFFERTY: This is why we have not seen the academic field. But as you know, in the world of economics there are two schools. There is the classical orthodox school in the marketplace and there is the school of the new economics.

The CHAIRMAN: Yes.

Mr. LAFFERTY: The new economics rebel very strongly in the academic field, both in the United States and here, and those who are orthodox in the marketplace are not in entire harmony with them.

The CHAIRMAN: You think that is part of a plot?

Mr. LAFFERTY: No.

Mr. LIND: Mr. Chairman, is Mr. Lafferty suggesting, when he mentioned the School of Business Administration at the University of Western Ontario, that they do not teach anything about the inner workings of the banking systems because they are biased or afraid to do so?

Mr. LAFFERTY: I did not suggest that Western University did not teach this; I suggested that in Canada the only one that had become recognized for its competence in the marketplace so far is the one of Western University.

Mr. LIND: Well is this not one of the evolutions of education, that it progresses?

Mr. LAFFERTY: It has been a lot slower here than it has been south of the line.

Mr. LIND: It has more case histories and it knows more about the financial institutions of our country. I do not think they refuse to teach it.

Mr. LAFFERTY: I have not suggested that they refuse to teach it.

The CHAIRMAN: Are you suggesting, for example, that Queen's is not a competent faculty in this field?

Mr. LAFFERTY: No, I am not suggesting they are not competent.

The CHAIRMAN: Mediocre?

Mr. LAFFERTY: No, I do not think one could make a judgment in those terms without making a comparison with all those that are available.

The CHAIRMAN: Have you not done this in your statement?

Mr. LAFFERTY: We have suggested that the conditions exist that have created this kind of set of conditions.

The CHAIRMAN: Then you must be including Queen's.

Mr. LAFFERTY: I am including all universities. I suggest that you take students from these various faculties. Your function is to investigate; it is not mine. My function is to express a dissenting viewpoint. As I expressed before, I do not have the powers, the staff or the financial means to do the kind of examination and produce the evidence you seek. It is your function.

The CHAIRMAN: We carry out our investigations by listening to witnesses who make statements.

Mr. LAFFERTY: If I may suggest, this is not the way to do it.

The CHAIRMAN: You are a witness and you are making a statement.

Mr. LAFFERTY: Sir, if I was in research and I was to accept anything that was told to me, I would certainly want to investigate to see if there was any validity in that which was expressed to me.

The CHAIRMAN: After listening to you, I can agree with that.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I have a supplementary question for Mr. Lafferty. You refer to yourself as a financial analyst. I wonder if you could give an ignorant person like myself an idea of the sort of work you undertake. It might then give us some idea of your connection with the financial world and your ability or insight into the operations of the financial world of banking. I do not quite know what functions your firm performs.

Mr. LAFFERTY: We are basically in what we term the investment research field. Our function is to be able to interrelate. We accept as a basic premise that all economic conditions are created by political decisions, whether it be the monetary field, fiscal field, taxation, or whether it be import-export. Therefore, we relate the influence of political decisions in the economic field. To go further, we interrelate the consequences of these decisions in the economic field to the individual companies, which are represented by stocks and shares listed on the various exchanges because they are public companies. It is our function to advise people whether an investment is a favourable position or an unfavourable position in relation to these over-all set of conditions. We are therefore, very extensively absorbed, shall I say, in the international monetary field, the local domestic field, corporate life and financial aspects of the community. In our particular instance we sell professional appeal. The work which we do is considered very professional, very sophisticated and, in part, past and beyond the reach of most of the public. We do not seem to sell to laymen. Because we service somewhere in the area of 100 financial institutions, we have a reasonable exposure to growth and understanding. We have survived in this marketplace on what we have been able to do so I assume that we serve a useful purpose.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I was not suggesting that you were not. I hope you realize that it was from ignorance that I asked the question. Would it be right to say that you are in some regard an investment consultant?

Mr. LAFFERTY: We act in the field of investment consultants as well. We have a firm in the investment counsel field. What you gentlemen perhaps do not realize is that if you have collusion and conformity in the marketplace, the person who is primarily exploited is the investor. He cannot judge this. If your function is to protect the investor, then you cannot conform to the rest of the marketplace if it is not moving correctly on some principle. If it is moving in the direction of collusion or seeking to achieve certain things, price levels or stipulations, then you have to make up your mind whether your function is to serve the consumer or join that group of conformity who are seeking to either preserve, protect or pursue their own ends and objectives. Our function is to serve the consumer, who is the investor.

Mr. LAFLAMME: Mr. Lafferty, would I be right in saying that the main purpose of your brief is to put forth the thought that you would like to see more competition among financial institutions?

Mr. LAFFERTY: I do not know to what extent you gentlemen are aware of the capital markets in Canada, but the capital markets in Canada are sick. We have had a series of situations Windfall, Atlantic Acceptance, Prudential Finance, Alliance Credit, Laurentide Finance. These are symptoms of a set of conditions; these are not accidents of occurrence. They are symptoms of a condition whereby the Canadian capital markets will be dependent now on borrowing from others.

Mr. LAFLAMME: At page 10 you state:

It is a system of graces and favours where the consumer is given what he can get, and in many instances must prostitute himself for that which he receives.

What is behind that? Do you have anything to say regarding anything that is wrong. Graces and favours mean the banana republic and if you have anything to tell us regarding this system, please do so.

Mr. LAFFERTY: Once you have a cartelized structure, the consumer does not have a freedom of selection and, therefore, he must make a deal in which he seeks to participate, to restrict his freedom of choice.

Mr. LAFLAMME: What do you suggest to avoid this system of graces and favours?

Mr. LAFFERTY: This comes back to the underwriting matter that I discussed previously. As long as you have non-competitive underwriting in this country, a necessity for that which is underwritten, and others are dependent on that product and they have no freedom or range of choice, then you have this problem, the same as you have in any cartelization.

The CHAIRMAN: Then you are also calling for changes in the security laws? For example, you would propose a change to require competitive bidding on underwriting?

Mr. LAFFERTY: As I have pointed out, in the United States a bank is not permitted to underwrite corporate areas. This was broken up many years ago, resulting in the same set of conditions that is felt now in Canada. The influence of banks is such in the financial community that they dominate it and they no longer have free capital markets.

Mr. McLEAN (*Charlotte*): Mr. Chairman, I have a few questions. You seem to think that our capital markets are sick in Canada. If they are not sick in the United States, why are United States companies going over to Europe to borrow \$500 to \$800 million.

Mr. LAFFERTY: Because there are more borrowers than funds available.

Mr. McLEAN (*Charlotte*): Why is Douglas running around trying to get finances at the present time?

Mr. LAFFERTY: If he did not have credit problems, I am sure he would not have any difficulty.

Mr. McLEAN (*Charlotte*): I know, but if they have these markets in the United States and are so superior down there, why does Douglas have to run all over the place looking for someone to bail him out?

Mr. LAFFERTY: Because there is a higher rate of risk than those lenders in the States are prepared to undertake.



Mr. McLEAN (*Charlotte*): You suggested that you are in the international field.

Mr. LAFFERTY: I said we were exposed to it.

Mr. McLEAN (*Charlotte*): If you are in international finance, can you tell me why \$35 American in 1945, when the international monetary fund was established—I am sure you are familiar with it—was equal to an ounce of gold?

The CHAIRMAN: Well Dr. McLean—

Mr. McLEAN (*Charlotte*): Just a moment; he said he was in the international field.

The CHAIRMAN: I realize that, and I am not saying this is not a useful area.

Mr. McLEAN (*Charlotte*): I would like to get this answer.

The CHAIRMAN: I will permit the witness to answer, but I thought that we were in the general area of discussing Mr. Lafferty's proposal that an officer of a Canadian chartered bank should not serve as a director of the corporation. We strayed a bit from the specific point because it related to some comment that he made in the general discussion prior to this brief.

Mr. McLEAN (*Charlotte*): He told Mr. Cameron that he was in the international monetary field.

Mr. LAFFERTY: No, I did not say that sir; I said that we were exposed to the international monetary field.

The CHAIRMAN: If you care to make a brief comment on this, Mr. Lafferty, you may do so; if not, I think we should consider whether we have any further questions on the very useful proposal to ban officers of banks from being directors of corporations, and then move on to the next group of proposals about proxies and so on.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Lafferty, you spoke of the precedent set by the Bell Telephone Company, its financing by the vehicle among the banks and an affiliated or an associated concern. How do you think that the prohibition of joint directorships would prevent a similar arrangement being made which presumably would be to the advantage of those who made the arrangement?

Mr. LAFFERTY: I think perhaps we did not have an interrelating board on the Bell Telephone. The Bell Telephone board fulfilled an obligation that they should go into the marketplace and take competitive business.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But if they could find a bank which would be prepared to do this for them, I have no doubt that they would be able to do it without too much difficulty. If they have already found one, they would find another would they not?

Mr. LAFFERTY: But they would find it at a more competitive rate.

The CHAIRMAN: Perhaps we could group the next three proposals together: the two proposals about formal proxy and the one about increasing the number of times banks should be required to report to shareholders. We have seen these proposals. Are there any questions relating to one or all of the three? This is

consistent with a number of proposals along these lines by some of our other witnesses, including some of the academic ones. Do we have any questions on these?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I have one question. Do you think, Mr. Lafferty, that the disclosure of all outside directorates held by nominees would affect the election of a candidate as a bank director?

Mr. LAFFERTY: All I suggest, Mr. Chairman, is that the shareholder would be more informed.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would it not be more likely to pump for the fellow who has a whole lot of directorates?

Mr. LAFFERTY: It might be his choice, but this is up to the shareholder. Some shareholders might think that the more directorates he had the better; others might suggest that the more he had the less value it would be to them or to a greater extent, he might compare one with another.

Mr. ADDISON: Mr. Chairman, could I ask one question. Do you feel that an employee of a government agency or a director of a crown corporation should be a director of a Canadian chartered bank?

Mr. LAFFERTY: No, I do not.

The CHAIRMAN: Do we have any questions on the proposal with reference to section 76, about banks owning shares of corporate stocks or other entities. In other words, would you forbid a bank even owning 10 per cent of an entity such as Roy Nat?

Mr. LAFFERTY: Yes.

Mr. LAMBERT: Why?

Mr. LAFFERTY: Because the function of a bank is to carry on the banking business, and I think they should stick to their business.

Mr. LAMBERT: Is Roy Nat not part of the banking business, to come down to a specific example?

Mr. LAFFERTY: It is part of the banking business, to be incorporated in the bank; it is not part of the banking business—

Mr. LAMBERT: I notice in your brief you object to the sale of debentures by banks and you object to the proposal here that they shall enter into what you would call the medium length field of financing.

Mr. LAFFERTY: I do not think there is any restriction in the Bank Act against medium length financing by banks.

Mr. LAMBERT: Well this is where the access of funds arises. There is the question of liquidity and what have you, and ordinary prudent practice.

Mr. LAFFERTY: I think if you look at some of the major banks in the States you will find that 70 per cent of their loans are term loans—term loans exceeding five years and probably seven in some cases.

Mr. LAMBERT: That may be but I am not overly concerned about the banking practices in the United States.

Mr. LAFFERTY: The use of this is an exception.

Mr. LAMBERT: In Canada it had not been the practice. In fact, it just was not possible, and this is one of the things where you get yourselves in terrible trouble. A lot of the present near-banks have got themselves in trouble. They have loaned on long-term money that they had to get on short-term. Is it not a prudent practice that if you are going to go in for demand deposits then you will be lending on short-term and if you are going to lend at longer term then you get money that is available to you under three, five or maybe a longer term than that.

Mr. LAFFERTY: Generally you arrange a loan in relation to what your term and deposits were. You can take deposits of funds for one year, two years or three years of 30 days.

Mr. LAMBERT: It is conceivable that a bank in the present context could actually still carry on its activities in a corporation like RoyNat, if it sees fit?

Mr. LAFFERTY: Is this not a judgment of the legislature? It is question of whether it is desirable or undesirable.

Mr. LAMBERT: No. If it is within its powers contributing to the economic development by furnishing financing to legitimate business interests, what is wrong with that?

Mr. LAFFERTY: If it could do it within the provision of its Bank Act legislation there is nothing wrong with it. If it does go outside that legislation to do it then what is the purpose of the legislation.

Mr. LAMBERT: Well whether it does it directly or through a subsidiary, what is the difference?

Mr. LAFFERTY: Well, it is only if there is some reason for doing it through a subsidiary.

Mr. LAMBERT: It serves the end of the consumer to have this facility, which is a point which you emphasized time and time again.

Mr. LAFFERTY: It does not conform with the Bank Act. Is it not a translation of the spirit of the legislation, the intended purpose of the legislation?

Mr. LAMBERT: No, it is a question of the interest rate and the term of the lending and that is all.

Mr. LAFFERTY: Well there is no reason the banks should not pay 7 per cent on deposits if they wished to do so.

Mr. LAMBERT: Except that it cannot lend any higher than that. Why would you eliminate equity stocks from a bank's investment portfolio?

Mr. LAFFERTY: Not from an investment portfolio; from an operating position, yes, because I think they should stick to banking.

Mr. LAMBERT: We know that banks have investment portfolios, this is so.

Mr. LAFFERTY: True.

Mr. LAMBERT: But I think that your absolute prohibition here would eliminate an investment portfolio of equity stocks.

Mr. LAFFERTY: You mean equity stocks in the portfolio itself?

Mr. LAMBERT: Yes.



Mr. LAFFERTY: Yes, I am personally opposed to them.

Mr. LAMBERT: Why?

Mr. LAFFERTY: I think if you look at the German banking system you will see a large cartelization of most of German industry is controlled by the banks. If you go back to the early history of national socialism you will probably find this is from a concentration of these equities and interest of ownership in the three major banks in Germany. The vacuum that is created therefrom and the lack of distribution amongst the population as a whole of the ownership of industry.

Mr. LAMBERT: All right, you have cited a German example, but the banks have been entitled for years now to own equity stocks in Canada. You propose a ban; in other words, a change. Now what evidence have you that this has operated to the detriment of either the Canadian economy or the Canadian banking field.

Mr. LAFFERTY: In banks in Germany—

Mr. LAMBERT: I am speaking of Canada.

Mr. LAFFERTY: All right; let me explain. Banking in Germany has had the effect that a bank can influence price structures in the market. The same principle could apply here. So friends of a bank with a large holding position of equity of common stocks could make an influence on price structure of the market without any disclosure.

Mr. LAMBERT: But, has it happened?

Mr. LAFFERTY: I do not have access to records of the banks.

Mr. LAMBERT: What are we getting at?

Mr. LAFFERTY: I explained the principle, Mr. Lambert. I am not expanding the incident.

Mr. LAMBERT: Are you giving us series of Aunt Sallys here or men of straw—

Mr. LAFFERTY: It is the principle of the golden wire.

Mr. LAMBERT: —bogeymen that you may want to raise without any evidence? I mean you are proposing certain changes and I put it to you, Mr. Lafferty, that if you want changes, then the burden of proof for those changes is upon you.

Mr. LAFFERTY: If you read the brief maybe you—

Mr. LAMBERT: I read the brief but wide statements made by you is not evidence as to the validity of the position you take.

Mr. LAFFERTY: No; the validity of the position I take is only on the reasoning which is submitted. You may reject it.

Mr. LAMBERT: All right.

The CHAIRMAN: I think Mr. Lambert is referring to the fact that you are a financial analyst and you do work for a hundred institutions.

Mr. LAFFERTY: We do not work for a hundred institutions; we serve a hundred institutions.

The CHAIRMAN: What is the difference?

Mr. LAFFERTY: One would suggest that we were an employee.

The CHAIRMAN: I see. I gather you have access to a very wide range of factual material; I would have thought you would have been in a position to materially assist the committee by bringing this factual material before us.

Mr. LAFFERTY: Mr. Chairman, I do not know what your exposure is to financial markets or the financial community but a great deal of what takes place in the financial community is by word of mouth. Most contracts and transactions are by word of mouth, by telephone conversations or by personal discussions with two or three people. These are normally considered of a personal and confidential nature. If I happen to be aware that something took place I have no right to implicate somebody else. I am also acting in a fiduciary capacity. I know what the consequence of what we decide to do will be and I also probably know the motives. The purpose behind this brief is to try and prevent some of the shenanigans that take place from taking place. But I cannot go and indict those people, bring them on the witness stand and relate this to a conversation which took place a year ago.

The CHAIRMAN: You have parliamentary immunity by being before this committee.

Mr. LAFFERTY: Thank you.

The CHAIRMAN: What I am driving at, sir, is that you have facts which you feel if you give them out of context might be used against you. If they really are facts, this might be a wonderful opportunity to strike a blow for improvement of the situation.

Mr. LAFFERTY: It is not practical.

The CHAIRMAN: Do you have any further facts to give us?

Mr. LAFFERTY: On what?

The CHAIRMAN: To support some or all of these statements.

Mr. LAFFERTY: These are made by reasoning of the whole theme of the philosophy behind the brief. Now if you take the actual proposal out of this context, then they are out of relationship of what the whole intent of the brief was. But this is your choice. It is not my function to impose my views on you but to try and explain to the extent I can.

Mr. CHAIRMAN: No, you are performing a useful function.

Mr. LAFFERTY: More than this I cannot do.

The CHAIRMAN: This may be a matter of semantics. Perhaps I interpret words differently than you do, but a lot of things in your brief are not in the form of suggestions, probabilities or possibilities but flat statements, and I would have thought that you would have been in a position to back these things up.

Mr. LAFFERTY: Let us start off first with this. You have an interlocking set of factors which were filed as a list in one of the hearings you had. My view is that for a hearing of this nature and for the problem with which you are faced a proper relationship should be made of the various institutions, not just a list of directors and which are which, but how they come, how they relate and what it

means in the colony as a whole. But there seems to be no evidence that this kind of preparatory work has been prepared for the committee. This is the function of those who are responsible for preparing the basic pattern of the committee.

The CHAIRMAN: I think you should be aware that our committee structure has not evolved as yet to the stage of the American system and we must operate to the best of our ability within the context of—

Mr. LAFFERTY: But you cannot ask me to accept the deficiency.

The CHAIRMAN: But why not sir?

Mr. LAFFERTY: Because it introduces implications in which I am not going to become involved. I am a private citizen; I cannot start indicting, accusing people or introducing evidence which does not belong to me.

The CHAIRMAN: In other words, you can indict the system—

Mr. LAFFERTY: All I am involved with is the system.

The CHAIRMAN: But you are not prepared to give evidence to support your indictment.

Mr. LAFFERTY: No. I am prepared to give the reasoning behind the principles, yes, and they are in here. But I am not prepared to provide individual incidents, the personalities involved and what took place, and relate them.

The CHAIRMAN: Do you have knowledge of such incidents?

Mr. LAFFERTY: If you are exposed to a financial community for ten or fifteen years you have a pretty extensive knowledge.

The CHAIRMAN: Personal knowledge?

Mr. LAFFERTY: Oh sure I do; I am bound to.

The CHAIRMAN: And you are not going to tell us about them?

Mr. LAFFERTY: It is not mine to tell, and I could not prove it anyway.

The CHAIRMAN: You could not prove it?

Mr. LAFFERTY: No. All I could relate was what took place. I tell you most financial transactions in the financial community are done by word of mouth. They are not written into agreements or contracts.

The CHAIRMAN: Do we have any further questions on the proposal regarding clause 76, which is with respect to the limitations on a bank owning shares of other corporations. If not, I would like the committee to pose any questions they have on Mr. Lafferty's proposal regarding interest rate ceiling.

Mr. CLERMONT: According to your brief, Mr. Lafferty, you are against a rate ceiling?

Mr. LAFFERTY: Yes.

Mr. CLERMONT: Even in the situation we are in these days with a tight money situation, you are still against a ceiling?

Mr. LAFFERTY: Sure. With proper competition then those which have merit for borrowing will buy or borrow at certain rates and those that have less than that will pay a higher rate.



Mr. CLERMONT: What do you mean by proper competition, an eight, nine or ten per cent rate?

Mr. LAFFERTY: Is your question, what rate would result if you had proper competition?

Mr. CLERMONT: Yes.

Mr. LAFFERTY: I would say you have reasonable competition in the United States at the present time and in a large number of European countries. The rates will adjust or level to what the market demands or what the market is willing to pay for.

Mr. CLERMONT: Are you aware of any bank commercial borrowing rates in the United States?

Mr. LAFFERTY: They vary all the way through the States. I do not think you can arrive at a specific figure along those lines, Mr. Clermont.

Mr. CLERMONT: Have you any figures, say, regarding New York State?

Mr. LAFFERTY: What the borrowing rate is?

Mr. CLERMONT: Yes.

Mr. LAFFERTY: It varies from one bank to another but, as you know, there is a prime rate published.

Mr. CLERMONT: If different banks have different rates where is the competition?

Mr. LAFFERTY: It does not exist here at the present time.

Mr. CLERMONT: I mean in the United States?

Mr. LAFFERTY: Oh yes, I think there is a range of different rates.

Mr. LIND: Mr. Chairman, at the bottom of page 29 in the opening statement you ask that the interest rates to be freed. Then you say:

It is the responsibility of Government and legislation to see that those markets are properly regulated, free from fear and intimidation, and equally accessible to all participants without regard to the creed or class to participate if they should so wish.

Is not our present banking system, where we have a controlled interest rate, accomplishing what you ask for in that paragraph?

Mr. LAFFERTY: I do not think so.

Mr. LIND: Well how is it not? Where are the difficulties? Can you give us an example? This is what I am concerned about.

Mr. LAFFERTY: It reads:

It is the responsibility of Government and legislation to see that those markets are properly regulated, free from fear and intimidation, and equally accessible to all participants without regard to the creed or class to participate if they should so wish.

It seems clear to me. Is it not clear to you?

Mr. LIND: Well, no; I have never known banks to create any fear or intimidation in people.

Mr. LAFFERTY: I have suggested and my own experience is that they do exercise an influence both favourable and unfavourable in the financial community, depending on what their interest, pursuits and motives are.

Mr. LIND: Do you mean they are going around scaring people, intimidating them or what?

Mr. LAFFERTY: I would suggest that this is an indirect result of a set of conditions, yes.

The CHAIRMAN: Some customers may feel that way once in a while, perhaps wrongly, sometimes rightly.

Mr. LAFFERTY: If you would like me to pursue that a little further I will bring you some evidence.

Mr. LIND: I would like to hear the evidence.

Mr. LAFFERTY: All right. In my original notes and summary I presented to you an idea or the thought that the conditions that led into the stock exchanges were a result of this over-all dominant position of interest. We published two years ago a brief on *The Correct Role of the Stock Exchange in a Free Enterprise Economy* in which we outlined the principles under which the stock exchanges in Canada should be operating. Because this challenged the dominant interests we were charged by the stock exchanges for having published such a pamphlet. We were tried by a Kangaroo Court; prosecuted by the leading counsel, a director of one of the leading major banks, and we were found unanimously guilty for acting in a manner unbecoming to a member of the stock exchange because we publicly disclosed that the stock exchange was operating badly. If that is not intimidation and fear then I do not know what is.

The CHAIRMAN: What penalty was imposed?

Mr. LAFFERTY: I would be glad to make copies available of this particular pamphlet. It is called "The Correct Role of the Stock Exchange in a Free Enterprise Economy."

The CHAIRMAN: Perhaps you could distribute copies separately to the members.

Mr. LAFFERTY: If you want the evidence there it is.

Mr. LIND: What about the general public; do they intimidate them?

Mr. LAFFERTY: It goes down to those who act for the general public.

The CHAIRMAN: Mr. Lind, do you have any further questions?

Mr. LIND: It is the government's responsibility to see that the consumer is not exploited by cartels and agreements of collusion. If you free the interest rate which acts as a control, then you expect the government to add other controls. Now, what controls do you suggest.

Mr. LAFFERTY: You take away the interest rates but you also prevent collusion and intimidation.

If you allow free enterprise, proper anti-combines and anti-trust legislation takes place, then the natural demand and supply will adjust in its own field without any intervention by the government. You do not require a government

regulation then. But if you do not have those in play then you have some exploited at the expense of others.

The CHAIRMAN: You are also suggesting that there is room for strengthening our anti-combines legislation.

Mr. LAFFERTY: Yes. I think we have already suggested and discussed this.

An hon. MEMBER: In what respect would you strengthen this?

Mr. LAFFERTY: I understand at the present time it is completely ineffective. We already have the evidence of the combine of George Weston, the Argus Corporation and Canadian Breweries who were taken to trial by the government. It was defeated in the court and therefore it did not stand up. The anti-trust and anti-combine legislation in the United States opens the framework of the economy, which allow for new ideas, growth of the small corporations and the vitality which affects a lot of the United States economy, which we do not have.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Do you think the anti-trust action against the Standard Oil company really has had the effect of separating that octopus into separate tentacles?

Mr. LAFFERTY: Oh, yes, I think so to a large extent. I would say Standard Oil of Indiana was a very effective, self-contained unit operating on its own merits and its own abilities. I would say Standard Oil of New Jersey and of California had similar individual identities.

The CHAIRMAN: Now, finally to conclude this reference to page 30 of Mr. Lafferty's brief, there are three points. Are there any questions on these three points? There is the suggestion that the Act should clearly define interest, which is something that we have raised ourselves here on numerous occasions; there is also a suggestion made that the Bank of Canada should take over the clearing operation, and finally that membership of any officer or director in any association providing the facilities for collusion should be prohibited. Are there any questions on any of these three points?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I think, perhaps the last one sets forth a very admirable objective. Are you going to prohibit membership in clubs of various sorts to officers and directors of banks. Are you going to place them into "monkish" cells.

Mr. LAFFERTY: No; I think clubs are in the area of each individual's right to socially habitate.

The CHAIRMAN: You say "facilities". What do you mean by "facilities"?

Mr. LAFFERTY: I think the Bankers' Association is a facility created by parliament. I do not think that should be so.

If I may, I would like to bring up this particular point. There are some figures submitted by the Bankers' Association on the invested index of bank shares and it shows an annual growth of two per cent. They take the figures from 1959 to 1964, and I think they are misrepresentative. If you take the figures from 1954 to 1964, the average growth rate was nine per cent and not two per cent as depicted. They also reflect in their brief the benefits invested and not derived in those bank shares in that particular period. I think that should be more correctly



stated for the ten year period involved rather than a selected period of a few years, suiting the evidence being presented.

The CHAIRMAN: You refer to facilities for collusion. Are you referring to dining facilities?

Mr. LAFFERTY: No; the Canadian Bankers' Association which is a facility created by legislation.

The CHAIRMAN: You refer to a membership in an association providing the facilities for collusion.

Mr. LAFFERTY: It does provide facilities. It provides the framework and the roof under which it can take place.

The CHAIRMAN: I think that someone could read that suggestion of yours and think of a club with dining facilities.

Mr. CLERMONT: Mr. Chairman, number 2 states that the Bank of Canada should take over the operation of clearing cheques for all of the banks. When the Governor of the Bank of Canada was questioned on this, if I recall correctly, it seems to me that he did not have the facilities and he did not see his way clear to operate such a clearing house because to do this he would have to open offices throughout Canada.

Mr. LAFFERTY: Mr. Clermont, is this an impossibility.

Mr. CLERMONT: No, it is not an impossibility but there is always the question of cost. By No. 2 do you mean that it is not possible for any institution to have the facility of a clearing house.

Mr. LAFFERTY: In my own view it gives these hands too much power. This should be in the hands of a neutral source or a neutral forum.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Would you include in this all institutions which grant checking privileges whether they are officially banks or not?

Mr. LAFFERTY: Yes. I think it provides a convenience and an entrance to them which protects their own business without transgressing into the affairs of their own development.

The CHAIRMAN: Are there any further questions on these three final suggestions in Mr. Lafferty's original brief? If not, we should turn to his subsequent brief because he makes a number of very interesting suggestions and points.

May I make a suggestion to the Committee? We have a meeting scheduled for this evening and our third witness today, Mr. Howes, has a brief which is more limited in size or length than Mr. Lafferty's. Perhaps it would be the most fair way to deal with Mr. Lafferty's further submission if we took a little time this evening since we are going to sit anyway. At that time we can consider them and not try to rush over them in a few minutes. If that is agreeable to the Committee perhaps we might recess now and resume this evening so that we could have more time for further consideration of the addendum.

I declare this meeting recessed until 8.00 p.m.

## EVENING SITTING

The CHAIRMAN: Gentlemen, I think we are in a position to resume our meeting. When we recessed for supper we were about to see if the Committee had any questions on the proposals made by Mr. Lafferty in his further memorandum of September 6, 1966. There are a number of specific proposals or views which begin on page 3 of the memorandum. In the first one Mr. Lafferty criticizes the proposal in the new bill that banks be permitted to form executive committees at the board level to act for directors, and he gives his reasons. Are there any questions or comments on this point? If not, we shall pass on to paragraph 2 on page 4. Mr. Lafferty makes a number of proposals to the effect that the bank reporting, with regard to the items mentioned, be consistent with the new Canada Corporations Act. I think I have summarized that appropriately. Those are the first two, and the third one is also a suggestion that insider transactions be disclosed in a manner consistent with the new Canada Corporations Act and the new Ontario securities legislation. I think I have also summarized that appropriately. Are there any questions or comments?

Mr. LAMBERT: I have one brief question. With regard to the salaries of officers, how far down the line would you go, Mr. Lafferty, in your recommendation? The executives extend rather far down the line, to regional assistant managers, and so forth.

Mr. LAFFERTY: Are they officers of the bank under the new structural organizations? I do not think so.

Mr. LAMBERT: Well, do you mean to say—

Mr. LAFFERTY: The officers of the bank would be the corporate officers, or the bank officers, officially designated.

Mr. LAMBERT: Just within the directorship?

Mr. LAFFERTY: Who are officers of the bank.

Mr. LAMBERT: I see. That is a clarification.

Mr. LAFFERTY: Yes, I think this is normal corporate practice.

Mr. LAMBERT: All right.

The CHAIRMAN: Are there any further questions on this section 2?

In the third paragraph on page 5 Mr. Lafferty criticizes the proposal that the chartered banks be allowed to issue debentures. Are there any questions on this suggestion?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Chairman, I should like to have further elaboration from Mr. Lafferty on that point.

Mr. LAFFERTY: Certainly. If one goes back a little further to the earlier evidence one can see the tremendous dominance banks have in the financial community. This means that they could place those securities, whether or not they were merited on the basis of valuation of the assets, because of their dominant or influential position in the distribution of securities. The second question is whether it is desirable. Canadian banks already have a major part of Canadian savings. Should they be further expanded at the disadvantage of others who would like to compete in this market on a basis of merit rather than on a basis of power to influence and distribute the securities?

Mr. MORE (*Regina City*): Is it not a fact that the Canadian savings which the banks hold are diminishing year by year with the competition they have from near banks?

Mr. LAFFERTY: This is contended in the brief and I think their assets have decreased as the others have expanded. They maintain this is because they have certain disadvantages. Others would maintain it is because the near banks provide a service which the consumer accepts more readily than that service which they provide and therefore one is serving the consumer to a greater extent than the other and he expands accordingly.

Mr. CLERMONT: Are the American banks allowed to sell debentures?

Mr. LAFFERTY: Yes, they are. I am not sure that it prevails in all states. It certainly prevails in the state of New York and in the state of California.

Mr. CLERMONT: You are not sure if it is all states. Is there a national banking act in the United States?

Mr. LAFFERTY: There is both federal legislation and state legislation. It would depend under which you are.

Mr. CLERMONT: Yes, but is there a national banking act?

Mr. LAFFERTY: Yes, federal legislation.

The CHAIRMAN: There is no single statute. I think that is what you mean.

Mr. CLERMONT: What I mean is, is there any bank in the state which holds a national charter?

Mr. LAFFERTY: Yes; some hold a national charter and some hold a state charter, Mr. Clermont. It varies. It has advantages and disadvantages.

The CHAIRMAN: Are there any further questions?

Mr. GILBERT: Are you in favour of the banks going into mortgages, because this is a method of the banks—

Mr. LAFFERTY: Yes. I see no objections, if they want to employ their funds in this direction.

Mr. GILBERT: But is this not a method of getting funds for mortgages?

Mr. LAFFERTY: It is a method of getting funds for mortgages. Again, you come into the position that they, because of their influence in the market, are able to sell debentures and they can then consolidate the funds; whereas if the depositor is unsatisfied he may move out. In this case, the debenture buyer can only try and dispose of the debentures he has acquired in the market-place. I see no objection why there should be a restriction on the manner in which a bank uses its deposits.

The CHAIRMAN: What was your point, Mr. More?

Mr. MORE: Nobody forces anybody to buy bank debentures. They do it willingly.

Mr. LAFFERTY: Yes, but if you have this pervasive influence I think you do get an influence where people are persuaded to buy securities they would not otherwise be persuaded to buy in their own judgment.



The CHAIRMAN: Well, is this comment of yours consistent with your support of the concept of the action of the market-place instead of government regulation?

Mr. LAFFERTY: Yes. I would like to pursue that a little further because you asked for evidence. This is a statement of a thing called the "Jockey Club". I do not know whether you are aware of it. We should also look at its capitalization. These securities were sold to the public. There was no justification at all. We can look at Argus in the same light. These were sold not on the basis of the merit of security. These were sold on the influence of the distributors who persuaded people to buy them.

The CHAIRMAN: You mean that the public was not using their own judgment?

Mr. LAFFERTY: You have a position here where the securities are distributed before the full disclosures are made or available and it is an emotional process of distribution. They are made hard to get with the intent of trying to excite the buyer into buying without a real knowledge of that which he is buying, because there is no prospectus.

The CHAIRMAN: What has this got to do with debentures?

Mr. LAFFERTY: Well, it was a question, which one of the gentlemen here raised, whether the buyer could exercise a free choice or not. I was merely explaining that this was not so.

Mr. MORE: He has a free choice when he buys them, has he not?

Mr. LAFFERTY: Does he have reasonable information from which to make a reasonable judgment? From my viewpoint of the distribution of securities in Canada, he does not because the prospectus is often available after he has to make a decision whether or not he should purchase them.

The CHAIRMAN: Would this be the case with bank debentures?

Mr. LAFFERTY: It would depend I guess whether they would be subject to the provincial securities commissions or not. I assume they would, whether the securities commissions insisted that the prospectus be properly prepared with full disclosure before anybody was approached on the sale of these securities. This would depend on that very much. In the United States you cannot do it until the prospectus has been prepared and has been delivered to the buyer or prospective buyer.

Mr. LIND: In the case of this "Jockey Club", is this not one of the stocks in which a fictitious, order to buy came on to the market from a bank in Nassau to the New York Stock Exchange on a Friday afternoon before Atlantic Acceptance crashed?

Mr. LAFFERTY: I do not know if the "Jockey Club" was in that group or not, I forget.

Mr. LIND: I think it was.

Mr. LAFFERTY: It may have been.

The CHAIRMAN: Are you finished, Mr. Lind.

Mr. LIND: I thought Mr. Lafferty could give us some information.

Mr. LAFFERTY: No, but if one wants to go under the pervasive influence of the dominant interests in the market you need to look at the board of directors of this and relate it to the Investment Dealers' Association and you will find there is quite a conflict of interest in this.

Mr. McLEAN (*Charlotte*): Mr. Chairman, I would like to ask Mr. Lafferty are these not good investments?

The CHAIRMAN: Which investments are you referring to?

Mr. McLEAN (*Charlotte*): The securities Mr. Lafferty referred to.

Mr. LAFFERTY: No, there are certain ratios and principles which one should apply to—

Mr. McLEAN (*Charlotte*): Are they good investments or are they not?

Mr. LAFFERTY: I do not think you can really reduce investing to that simplicity of terms. You could, in your terms place a value that may be—

Mr. McLEAN (*Charlotte*): The ordinary investor does not know one side of the balance sheet from another.

Mr. LAFFERTY: He has to learn.

Mr. McLEAN (*Charlotte*): Well, I know but he does not know.

Mr. LAFFERTY: Because the opportunity to learn is not there very often.

Mr. McLEAN (*Charlotte*): But he has got to depend on somebody else. He has got to depend on the character of the concern and the people behind it. The ordinary investor does not know what he is buying.

The CHAIRMAN: Can you answer, Mr. Lafferty?

Mr. LAFFERTY: He will be exploited.

Mr. McLEAN (*Charlotte*): Well, the first two investments I made I lost them. I made up my mind after that I would have to look into them.

The CHAIRMAN: You learned your lesson well, I understand.

Mr. McLEAN (*Charlotte*): Yes, well. The ordinary investor does not know what he is buying and there is no use to say all this because he does not know and he does not learn.

Mr. LAFFERTY: He will learn, Mr. McLean.

Mr. McLEAN (*Charlotte*): After he has lost it all and then he does not need any lesson after that.

Mr. LAFFERTY: If the facilities were there for him to learn, he would learn. I contend that the financial pages and the coverage we have in the financial press is not sufficient to properly inform him.

The CHAIRMAN: Mr. Lafferty, if the banks were forced by law to meet reasonable standards, standards satisfactory to yourself with respect to prospectuses and length of debentures, would you withdraw your opposition to banks issuing debentures?

Mr. LAFFERTY: No, I think you still contravene the original point. They already have a major proportion of the savings and they would use a dominant position to distribute, if they were allowed to distribute debentures without any difficulty, whether they had learned or not.

The CHAIRMAN: But you still do not think this is inconsistent with your point about free play in the market-place, with the purchaser if he wants to buy a debenture from a bank having the opportunity to do so.

Mr. LAFFERTY: He is probably building an image of the structure of the bank and its influence and its prestige, and you have a large number of what might be termed captive accounts and the trust companies are aware that they have sufficient influence that these things could be distributed.

The CHAIRMAN: I was going to suggest to the Committee that it was not fair to ask Mr. Lafferty to give his opinion on whether the two firms he referred to were good investments. After all, he makes his living selling this advice and I do not know if we should use our position to get this type of guidance.

Mr. McLEAN (*Charlotte*): He brought these firms up. I did not.

Mr. LAFFERTY: I brought them up as an example of financing, not as an example of investments made.

Mr. McLEAN (*Charlotte*): You brought the firms up. I think they are fair investments.

The CHAIRMAN: Well, we have your advice free, Mr. McLean.

Mr. LAFFERTY: I note what you say, sir, about free advice.

The CHAIRMAN: Sometimes it is very good. It depends a lot on the source. If it was Dr. McLean's advice there may be some who would take very serious cognizance of it, even though free.

Mr. GILBERT: Mr. Lafferty, if the trend were to have the near banks and other institutions come under the umbrella of the Bank Act you would then find that the near banks would have the power to issue debentures. They now have it; that is the way they obtain money for financing and investing. You would find that the banks would not have it and yet the trust companies would.

Mr. LAFFERTY: This is correct.

Mr. GILBERT: Would that be fair?

Mr. LAFFERTY: No, I am inclined to agree with you. It would not be equitable.

The CHAIRMAN: Are there any further questions?

Mr. McLEAN (*Charlotte*): Yes, I would like to ask Mr. Lafferty why are the banks issuing debentures? Is it not because we have a shortage of money? Is it not because the central bank is hauling in the credit of the country? Is that not it? Is that not the reason we have a shortage of money?

Mr. LAFFERTY: No. There is no question as to why the banks are issuing debentures because in their viewpoint they could acquire a larger position in their assets.

Mr. McLEAN (*Charlotte*): They cannot expand credit at the present time so they are going after any money that is available.

Mr. LAFFERTY: That is right. But it has to be at the expense of something else.

Mr. McLEAN (*Charlotte*): If they could expand credit they would not be going after this money, would they?



Mr. LAFFERTY: No. You cannot just continue to expand credit to satisfy the demand in the marketplace for credit without running into a lot of problems.

Mr. McLEAN (*Charlotte*): It is not the fact of the marketplace. We have the same conditions all over the world, not only in Canada. In Great Britain, in Germany, and in the United States, they have the same condition.

Mr. LAFFERTY: Yes, but Mr. McLean—

Mr. McLEAN (*Charlotte*): The Federal Reserve Bank is restricting credit in the United States and they cannot find the chairman at the present time. They tell me he is down on some southern island and they cannot find it.

Mr. LAFFERTY: But you appreciate that we have lost our freedom to make our own decisions in terms of monetary policy in Canada because we are dependent on the capital market in the United States.

Mr. McLEAN (*Charlotte*): We have lost freedom here in Canada because United States have lost their freedom, too.

Mr. LAFFERTY: No. We did not have to lose it at the same time.

Mr. McLEAN (*Charlotte*): They have lost their freedom.

Mr. LAFFERTY: No, we did not have to lose it at the same time.

Mr. McLEAN (*Charlotte*): They have lost it and they are trying to impose that loss of freedom on Canada.

Mr. LAFFERTY: No, they are not imposing it. We have put ourselves under obligation where we have to borrow or finance from them because our home capital markets are not sufficiently organized.

Mr. McLEAN (*Charlotte*): The United States owes \$30 billion in Europe which they cannot hide. That is the reason they have a balance of payments problem.

Mr. LAFFERTY: It is not entirely in Europe. It is largely in the Middle East and in Latin America.

Mr. McLEAN (*Charlotte*): It is in Europe. They have \$30 billion out in Europe.

Mr. LAFFERTY: Well,—

Mr. McLEAN (*Charlotte*): They have put \$70 billion out.

Mr. LAFFERTY: I do not think so.

The CHAIRMAN: Well, getting back to debentures—

Mr. McLEAN (*Charlotte*): I know it.

The CHAIRMAN: Are there any further questions or comments related more directly to Mr. Lafferty's views on banks issuing debentures? If not, I suggest we move on to paragraph 4 where he makes some interesting comments on the method under Bill No. C-222 for the incorporation or formation of new banks in Canada.

Mr. CLERMONT: What do you mean on page 6? This is a judgment that should be reserved to the market-place regarding new groups for banking.

Mr. LAFFERTY: It seems to me, this is to enable those who are sponsoring the creation of the new banks to have the respect and the support and the confidence

of the market-place. They will be waiting to find the funds or buy the shares and make deposits in that, and if they do not have the confidence it is just too bad.

Mr. CLERMONT: Under what guidance will they operate?

Mr. LAFFERTY: Under what?

Mr. CLERMONT: Under which guide will they operate?

Mr. LAFFERTY: They will operate under the Bank Act.

Mr. CLERMONT: According to you, they should not come to parliament for a charter.

Mr. LAFFERTY: This is correct.

Mr. CLERMONT: But as you know the banks are not the only financial institutions which have to come before parliament for charters.

Mr. LAFFERTY: I am aware of that. I do not think it should be necessary.

Mr. CLERMONT: Why? Is it because you think they have to use political influence?

Mr. LAFFERTY: I think they do.

Mr. CLERMONT: That is your own judgment.

Mr. LAFFERTY: That is my judgment.

Mr. CLERMONT: What have you to back it up? Is it the same argument that you had on other questions?

Mr. LAFFERTY: I have read the transcripts of the evidence of those who have applied for charters in the Senate.

Mr. CLERMONT: Parliament approved two new charters last year and I do not think any members were approached to sell their support.

Mr. LAFFERTY: The manner in which they had to achieve this would not encourage anybody else to try it.

The CHAIRMAN: What do you mean by that?

Mr. LAFFERTY: The long extended process, red tape and expense and cost to those who were sponsoring it.

Mr. LAFLAMME: I have a supplementary question. Do you know that only one member of the House of Commons can block the passing of a bank charter?

Mr. LAFFERTY: I was not aware of that.

The CHAIRMAN: Are you aware of the limited time available for any kind of private business in the House of Commons?

Mr. LAFFERTY: I have seen it. On Wednesdays, or something, is it not?

The CHAIRMAN: It is a little more frequent than that. Mr. Clermont, have you any further questions?

Mr. CLERMONT: No, that is enough.

Mr. LAFFERTY: Perhaps I may just qualify it by saying how it is done in the United States. A man does not have to go to congress in order to form or create a bank.

Mr. LIND: Nor to the state legislature?

Mr. LAFFERTY: I think not.

Mr. CLERMONT: I am moving to the next paragraph because according to it American banking is an ideal system and I would like to have a few explanations from you.

The CHAIRMAN: I do not know if we are finished—

Mr. CLERMONT: No, no, I am going to wait.

The CHAIRMAN: Yes. You refer to the market-place and suggest that the acceptance of a financial institution should be judgment reserved to the market-place. I should point out to you, sir, that the judgment of the market-place accepted Prudential Finance, Atlantic Acceptance and British Mortgage and Trust.

Mr. LAFFERTY: If there had been adequate information for the market-place to judge from these conditions would not have occurred. The proper legislation would have prevented it.

The CHAIRMAN: I might also point out that these three firms were incorporated by administrative letters patent procedure rather than by a legislative assembly.

Mr. LAFFERTY: Yes, I do not think that is the governing factor. I think the governing factor is that the information and the proper disclosure were not available.

The CHAIRMAN: I just wanted to point out to you that the system of administrative assent to issuing of letters patent by an administrative body is not necessarily a panacea.

Mr. LAFFERTY: Oh, no it is not. I agree, but I think in the earlier proposed legislation this qualification was not in. It was put in as an adjustment.

The CHAIRMAN: What qualification?

Mr. LAFFERTY: Of going to the legislature. It went to the Treasury Board, did it not?

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): In the former bill it was incorporated by act of the Treasury Board, I think.

Mr. LAFFERTY: Yes.

The CHAIRMAN: I just wanted to point out that—

Mr. LAFFERTY: It was a fairly simple and straight regulation. If they met the regulations then they could go into business. Whether they survived, that was their problem.

The CHAIRMAN: Would it not also be a problem for the depositors and the—

Mr. LAFFERTY: Certainly, the public at large. This is the essence of the market. They make their judgments, not some legislator.

The CHAIRMAN: You do not feel that the state should protect the small depositors, and so on.

Mr. LAFFERTY: Frankly, Mr. Chairman, I do not think the state is qualified.

The CHAIRMAN: In other words, you feel that we are not spending our time properly in attempting to set up a system which would protect the deposits of people who—



Mr. LAFFERTY: Mr. Chairman, you have no basic research data here. You have no evidence put together—

The CHAIRMAN: I am not talking about this Committee.

Mr. LAFFERTY: You asked me whether I think you are qualified or whether the state is qualified and I do not.

The CHAIRMAN: I am not talking about this Committee as such. I am talking about the state.

Mr. LAFFERTY: Yes, the state as a legislative function and this is part of its legislative function.

The CHAIRMAN: In other words, you are saying to us that we should not have new legislation providing for people like the Inspector General of Banking and—

Mr. LAFFERTY: Certainly, you should.

The CHAIRMAN: Well, you just said we should not be doing this.

Mr. LAFFERTY: No, I did not.

The CHAIRMAN: It sounded that way to me.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): May I ask you this question, Mr. Lafferty. You have some very strong views on the ways in which banks should be organized.

Mr. LAFFERTY: Not organized but governed; on the manner in which they should be governed by legislation.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Governed by legislation, yes.

Mr. LAFFERTY: The organization is an internal matter of management.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, that is what I meant by legislative organization. Now you are suggesting—I gather that you seized the opportunity to come before this Committee because you felt your views on it were valuable, and I think they have been. You would have had no such opportunity had the Treasury Board had the power to issue a licence; it would have just been done.

Mr. LAFFERTY: I did not presuppose or presume that my views would be as much as valuable to the Committee that I was a dissenting opinion and therefore I felt the dissenter should express his views, otherwise he could not justify his own position when he criticized the activities of the marketplace.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The point I want to make is this. I think you are too modest; I think your views have been very valuable and very useful to us, but you would have had no opportunity whatever to express your views had the provision in the previous bill before the house been passed as legislation.

Mr. LAFFERTY: As to making a judgment whether the banks should—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Of presenting your views to anybody at all.

Mr. LAFFERTY: I would have, surely under previous legislation.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I beg your pardon?

Mr. LAFFERTY: Under the original act before the—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Not if the bank charters were going to be issued by letters patent from the Treasury Board.

Mr. LAFFERTY: Oh, not with regard to the Bank Act.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): This was the proposal.

Mr. LAFFERTY: Not that the Treasury Board would govern the Bank Act; it was only the incorporation of new banks, surely.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, the incorporation of new banks.

Mr. LAFFERTY: I have no views on or judgment to make on whether or not banks are qualified to go into business. It is not my business. If I did have I doubt whether I could come to this Committee. I guess I could, but I do not think it would be my business.

The CHAIRMAN: This is a public hearing. Anyone can come forward and state his views on the public necessity or utility of incorporating—

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, but it is only because we have this sort of set-up that we are able to do it.

Mr. LAFFERTY: Mr. Chairman, my views have to do with the prevailing legislation governing the banks and not the men, or judgment whether or not one individual group is qualified to go into that business governed by that legislation. My views are on whether or not governing legislations forms a correct framework within which banks can operate in the interests of the majority of Canadians.

The CHAIRMAN: And you do not think it is in the interests of the majority of Canadians for the government to set up a framework to protect depositors against loss because of possible failure of banking and financial institutions?

Mr. LAFFERTY: This is going into another area which I do not think we have yet covered.

The CHAIRMAN: Well, you made a comment from which an inference could be taken—

Mr. LAFFERTY: Whether or not deposit insurance is a good idea?

The CHAIRMAN: I am not talking about deposit insurance specifically, but the concept of the state.

Mr. LAFFERTY: The state should govern the legislation. There is no question about that. The state should provide the legislation and include the legislation.

The CHAIRMAN: Are you now saying, contrary to what you appeared to have said before, that the state should also pass legislation to protect the depositor against loss of his deposits?

Mr. LAFFERTY: I never said that. You come into an area here where the state is subsidizing inefficiencies or delinquencies, which are inefficiencies, and it should not be put in the position of doing that.

The CHAIRMAN: You throw that on the individual depositor who—

Mr. LAFFERTY: Who should evaluate the bank's balance sheet and the bank's report sufficiently so that he can make a reasonable judgment.

The CHAIRMAN: You are saying that this should be done by a farm labourer or a factory worker?

Mr. LAFFERTY: He is probably going to be advised. He may go to his lawyer, or he may go to his accountant, but his accountant or his lawyer cannot advise him unless they have the recent background.

The CHAIRMAN: Do most farm labourers have lawyers and accountants?

Mr. LAFFERTY: I assume they are guided in their financial matters by someone, or else they depend on themselves.

The CHAIRMAN: I would think that it is a rather expensive lesson to face the risk of complete ruin.

Mr. LAFFERTY: Well, I think it would become knowledge within the community when a bank had published its financial position whether the position of that bank was good or not. The leaders in the community would identify it. At the present the leaders of the communities cannot because there is insufficient information available to do so.

Mr. LAFLAMME: Mr. Chairman, do you not really think that if someone in the Treasury Board had the right to give a charter to a new bank there would be a greater danger of favours, graces, political and financial influence among a small group than having banks organized by means of a private bill passed by parliament?

Mr. LAFFERTY: This could be, but I should hope not.

Mr. McLEAN (*Charlotte*): Mr. Chairman, on this—

Mr. LAFFERTY: Surely, when we go to the Secretary of State we want to incorporate a company. We do not have any problems at all as long as we meet the basic requirements. When you go to Treasury Board and you meet the basic requirements you should be authorized.

Mr. LAFLAMME: Any new bank will receive deposits and carry on business?

Mr. LAFFERTY: So long as it has the basic subscription of capital.

Mr. LAFLAMME: Do you not think it is safer for the public to have it organized as we do here?

Mr. LAFFERTY: I do not think it is any safer, no. I do not know exactly, but I do not think so.

Mr. McLEAN (*Charlotte*): The United States has this deposit insurance and there must be some reason for it.

Mr. LAFFERTY: Certainly there is.

Mr. McLEAN (*Charlotte*): I read in the papers where the daughter of the president, or something, goes off with a couple of million and the bank fails. How are the depositors going to know about that? I have read about at least three instances during the last year. Now, how is the depositor going to know about this? How are they going to know; do they have to take this risk?

Mr. LAFFERTY: No, I think there is a perfectly legitimate case, as you suggest, but my own view is that these are risks one takes in the marketplace oneself. When a man—

An hon. MEMBER: Are you putting these views forth seriously?



Mr. McLEAN (*Charlotte*): Sometimes a man who cannot even speak the English language—a foreigner—comes in and puts his deposit there and he loses it, and you say that he is responsible?

Mr. LAFFERTY: Well, he made a business judgment, did he not?

Mr. McLEAN (*Charlotte*): He does not know.

Mr. LAFFERTY: I do not know how you can ever state—I beg your pardon?

Mr. McLEAN (*Charlotte*): He cannot read a balance sheet.

Mr. LAFFERTY: Has he ignorance of the law?

Mr. McLEAN (*Charlotte*): He cannot read nor write.

Mr. LAFFERTY: Well then our education process is a bit backward.

An hon. MEMBER: You should start on that first.

Mr. LAFFERTY: In the United States they have 14,000 individual banks and many of these are in small communities where there is comparatively little knowledge; there is a protection that holds the structure together and prevents any scare-running or scare-run taking place on a bank, there is a knowledge that they are governed by an insurance depository system.

Mr. McLEAN (*Charlotte*): Sure, and they get that guarantee because they do not have a guarantee when they go into a small bank to make deposits. I think they are guaranteed up to \$10,000, are they not? If they are not guaranteed they go in and they have confidence and that is what we have got in our Canadian banks—we have confidence.

The CHAIRMAN: Are there any further questions on paragraph 4? If not, we will move on to paragraph 5; Mr. Clermont has already indicated he has some questions.

Mr. CLERMONT: Yes, Mr. Chairman. Mr. Lafferty says in paragraph 5 on page 6, that:

To our knowledge most of the Western nations permit the operation of foreign banks,—

Do you include in that the United States?

Mr. LAFFERTY: Yes.

Mr. CLERMONT: You are aware, for instance, that in the state of New York—if the information I have before me is correct—to open a branch, you must have a certain percentage of U.S. citizens as directors.

Mr. LAFFERTY: I do not know, Mr. Clermont, if that is a qualification you said it is; it probably is. I am not in a position to say whether or not it is a qualification.

Mr. CLERMONT: On what are you basing the statement that most of the western world permits the operation of foreign banks?

Mr. LAFFERTY: Well, you can go to Paris, you can go to Switzerland, you can go to the U.K., you can go to the United States, the state of New York, and these foreign branches and agencies are permitted.

Mr. CLERMONT: Yes, but if you open an agency in New York state you are not allowed to receive deposits from any resident of the state of New York.

Mr. LAFFERTY: It is my understanding that you may also have a branch in the state of New York.

Mr. CLERMONT: Yes, but with certain qualifications.

Mr. LAFFERTY: Yes, but you may have to have U.S. directors.

Mr. CLERMONT: And for the capital—

Mr. LAFFERTY: There is no reason why you should not make the same qualifications here if it is so thought desirable. I do not know what the merit of it is but I think it was more a nationalistic basis of—

Mr. CLERMONT: But again, according to the information I have before me, I think there is only one group that has obtained a national charter in the United States and they are not operating it. They may obtain a charter or a licence from individual states—not many; I think at the most eight or ten. I think over 40 states in the United States do not recognize or allow non-resident people to open a bank.

Mr. LAFFERTY: I think there are non-resident banks or branches of banks in the United States. I think we have stated that before.

Mr. CLERMONT: Yes, I agree, but not in every state.

Mr. LAFFERTY: No.

Mr. CLERMONT: Some of the states do not even recognize non-resident banking. In your brief you seem to be against the new bill.

Mr. LAFFERTY: I am against the exclusion of non-resident banks in the country.

The CHAIRMAN: Have you a question, Mr. Laflamme?

Mr. CLERMONT: That is all right, yes.

The CHAIRMAN: Mr. Laflamme.

Mr. LAFLAMME: Do you not think there is a great difference between foreign banks owned by U.S. people and foreign banks owned by other people, say, from Switzerland and other places?

Mr. LAFFERTY: No. I think if the French wish to come into Montreal and Toronto and run an efficient bank and serve the consumer they should be able to do so. If the U.S. came in and could equally, or more competitively, serve the consumer they should be afforded the opportunity to do so.

Mr. LAFLAMME: Yes, but there is a great difference between those two countries. We are very close to the United States and they are so rich that they could swallow us.

Mr. LAFFERTY: It is not a question of swallowing, it is a question of being able to compete on the ground.

Mr. LAFLAMME: How can we compete when we are the poorest?

Mr. LAFFERTY: I beg your pardon?

Mr. LAFLAMME: How can we compete with the Americans?

Mr. LAFFERTY: You compete not in terms of wealth but in terms of serving the consumer. If you can serve the consumer more efficiently you will obtain more business whether—

Mr. LAFLAMME: Do you really think that foreign capital will come into Canada to serve Canadian consumers?

Mr. LAFFERTY: Do not forget all the enterprises that were built with foreign capital—surely it does. This is the only basis on which they earn a profit.

Mr. LAFLAMME: Now, banking—

Mr. LAFFERTY: If a foreign bank wants to come into the country and serve the community it is up to them, and if they can make a profit at it, then this is effective.

Mr. LAFLAMME: And their main purpose will be to serve the consumer?

Mr. LAFFERTY: This is the only basis on which they can make reasonable earnings out of it, is it not? How else can they? They cannot tantalize the consumer. If they provide a service and he is willing to pay for it, either because it is a lesser cost than elsewhere or it is a service that was not available to him before and it is convenient and it is his choice to use it then why not? Why restrict the freedom of the consumer to make this choice?

Mr. LAFLAMME: Let us say, for example, that there are three foreign banks in Canada owned by Americans, and the American subsidiaries doing business in Canada decide to do business with their own banks. Do you not think this is going to affect our economy?

Mr. LAFFERTY: I do not think so.

Mr. LAFLAMME: Such decisions would be made in Washington?

Mr. LAFFERTY: I think they are already, because we are dependent on borrowing in the U.S. capital markets and our home market deposit is governed by this condition.

Mr. LAFLAMME: If they are already do you not think it is time to throw a curve?

Mr. LAFFERTY: But is this the way to do it? I think the way to do it is to make our banks self-sufficient so they can compete more effectively here so that foreigners coming in here cannot compete on our own home ground.

Mr. LAFLAMME: You said earlier in the afternoon that the banks are very influential in that field. Do you not think the Canadian government should have control of the banks?

Mr. LAFFERTY: No.

Mr. LAFLAMME: No.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Lafferty, the main burden of much of your brief has been your complaint, which I am—

Mr. LAFFERTY: Contention, if I may.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I beg your pardon?

Mr. LAFFERTY: Contention.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Very well, then. With regard to the contention you made which I rather regretted you were not able to document, that the banks practise a discrimination in favour of certain customers, do you not think that in a situation such as we have in Canada where a very



large proportion of our resource and manufacturing industry is in the hands of American capital that American banks here would attract to them in various ways much of the business of those allegedly Canadian companies which are actually subsidiaries of American companies?

Mr. LAFFERTY: Yes, they would, Mr. Cameron, but they are also able to do this without setting up banks here because all the major banks in New York have correspondents who come up here and visit with their companies and both solicit in periods of time when funds are available and solicit other conveniences and services they can provide. This takes place anyway, unless you are going to put a barrier against foreigners and decide that you are not going to allow any foreigners in here, but you are providing a banking facility for them to do it. I do not see where you have very much difference other than perhaps you are providing an additional convenience again to the consumer. You have some U.S. owned companies here who might find that the Canadian service was at a lower cost, more efficient and more convenient to them. I do not think the U.S. company is going to be swayed by nationalism. The U.S. company here is going to be swayed by what is its convenience.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): It might be swayed by the Rockefeller interests of New York, though.

Mr. LAFFERTY: Who will exercise pressure, there is no question about that.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, a very great influence.

Mr. LAFFERTY: They exercise large pressure. I do not know that this is specific to the Rockefeller interests, but certain U.S. interests do. There is no question about that. And so do the Canadians.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): The Rockefeller interests—

Mr. LAFFERTY: And so do Canadians.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): —are concerned with a particular bank.

Mr. LAFFERTY: And the Canadians do when they are in New York or elsewhere.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Yes, but not to the same degree. This is one mouse; one elephant.

Mr. McLEAN (*Charlotte*): Mr. Chairman, I should like to ask a question here. You say the American banks can do business now just the same as they did before, but they cannot on account of the interest charges. At the present time if we borrow in New York we have to account for the interest we pay to the banks in New York.

Mr. LAFFERTY: I am sorry, I do not follow it, Dr. McLean.

Mr. McLEAN (*Charlotte*): Well, I do not follow it either, but I could not borrow any longer in New York.

Mr. LAFFERTY: Let us say, Dr. McLean, I feel it is coming. My qualification is, if the funds were available.

Mr. McLEAN (*Charlotte*): The funds are available but it is a different proposition now because of the recent guidelines and all that sort of stuff they have brought in. You have to account to the income tax people in Canada for the interest you pay to the banks in New York, and this was not the situation before, so they are not on the same basis as they were 15 years ago.

The CHAIRMAN: Mr. Lafferty, as Mr. Clermont pointed out, when you say that to our knowledge most of the western banks permit the operation of foreign banks—

Mr. LAFFERTY: Most of the western nations, I think.

The CHAIRMAN: Yes, yes. You are surely not suggesting to us that most of the western nations permit unrestricted operations of foreign banks within their boundaries?

Mr. LAFFERTY: I do not know of any. There are local restrictions, I suppose. I do not know what the United Kingdom restrictions are on a non-resident bank. I do not know what the Swiss are, I think they are fairly free. I think in France they are governed by certain regulations because it is a pretty regulated banking and money market area.

The CHAIRMAN: Mr. Clermont, I think, pointed out to you that in approximately 45 of the 50 American states non-resident banking is completely banned.

Mr. LAFFERTY: Yes, but in the main—

Mr. CLERMONT: Let me correct that. I perhaps should not say banned, but they are ignored because they have a list and there are only eight states in the United States who have either agency branches, representation offices, state chartered subsidiaries and branches of state chartered subsidiaries.

Mr. LAFFERTY: There is very little point in putting a bank in Omaha, or something, and trying to develop business in the area.

Mr. CLERMONT: The "how" is not in that at all.

Mr. LAFFERTY: No. I say there would be very little point or incentive for a foreign bank to go and establish itself in Omaha.

The CHAIRMAN: The people in Omaha might feel that they were sufficiently established in the United States to—

Mr. CLERMONT: I do not see Las Vegas here.

The CHAIRMAN: As far as the United States is concerned it would hardly seem like a few limited local regulations.

Mr. LAFFERTY: I think this is an area where the committee should either, through the Department of Finance or the Bank of Canada, try and obtain this documentation of what the restrictions are so members can assess it. I do not say it is up to amateur witnesses like ourselves, but this is an area in which we do not have either need or call for complete documentation.

The CHAIRMAN: Once again you have made quite a specific statement, "to our knowledge most of the western—". Oh, I see, it is in so far as your knowledge extends?

Mr. LAFFERTY: Correct.

The CHAIRMAN: Is that what you mean?

Mr. LAFFERTY: To our knowledge. I think that is reasonable, is it not, as a qualification?

Mr. LIND: Mr. Chairman, Mr. Lafferty keeps speaking of the discrimination of the banks. What do you mean by discrimination? Are they discriminating between customers or are they discriminating between—

Mr. LAFFERTY: It is discussed fairly extensively in the basic text of the original brief.

Mr. LIND: I know.

Mr. LAFFERTY: The various bases of reasoning are given there. You can have discrimination in all sorts of different ways; business discrimination, discrimination in accommodation, discrimination in conveniences and discrimination in rates.

Mr. LIND: Do you not think it is a good part of the judgment of bankers to judge credit risks and allow different amounts of credit?

Mr. LAFFERTY: Let me put it this way. You ask for evidence of discrimination. Perhaps you would like to subpoena—I know you have the authority—the president of one of the major banks. We were cut off business from that bank by his direct instructions, and you can bring the branch manager who conveyed the instructions, because we published an article in 1964 which suggested that credit conditions in Canada were becoming loose. Now, Mr. Gibson, who is a knowledgeable banker and has already given you a transcript of evidence, has confirmed that credit conditions in 1964 were becoming loose. But because we stated this in a public report which was going to people who were professional in the field, we were identifying these conditions to them so they could avoid situations like Atlantic Acceptance, and everything of that nature, the big stick was waved over us and economic intimidation was imposed on us because we had reflected on this condition. Now, if you do not call that prejudice I do not know what you call it. I call it intimidation. I would like to subpoena the president of that bank and the branch manager concerned and take the oath of the witness and examine this with evidence. I have no qualms about it at all.

Mr. LIND: But you have an axe to grind, have you not?

Mr. LAFFERTY: I have no axe to grind.

Mr. LIND: But you are bringing up an examination—

Mr. LAFFERTY: You asked me for evidence.

Mr. LIND: I am asking you for evidence of discrimination other than your own.

Mr. LAFFERTY: What type of discrimination?

Mr. LIND: Well, I do not know. You speak of discrimination.

Mr. LAFFERTY: There is the whole context and the whole discussion of discrimination. You have discrimination going for that underwriting issue of Bell Telephone. It is all these selected dealers who are provided for in the distribution of those securities. This is not a competitive bid.

Mr. LIND: Well, is the Bell Telephone—



The CHAIRMAN: If we called the president and branch manager of this particular bank before us, as you suggest, would you also be willing to give us complete disclosure of your own financial condition at that time?

Mr. LAFFERTY: Or, sure. Any accommodation we have with a bank is fully secured. They have the security.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): In this instance you speak of with Bell Telephone, was this—

Mr. LIND: Mr. Chairman, can we have the president and manager of that bank summonsed?

The CHAIRMAN: Up until now most of the bankers have been quite willing to come here. In fact, some of them have been attending even when they did not have to be here. I think the best thing to do, if Mr. Lafferty perhaps would provide me with the names of the individuals in question would be to refer this to the steering committee and decide whether we want to pursue it further.

Mr. LIND: This discrimination which Mr. Lafferty mentions, Mr. Chairman, has rather given us a picture of bankers as being an iniquitous lot of people who dominate and plague and terrorize the average citizen. Do you seriously suggest, Mr. Lafferty, and I take this from what you said previously, that a bank combine or monopoly, or whatever you call it, was responsible for your prosecution by the Montreal Stock Exchange just because a lawyer who acts for a bank happened to act for the stock exchange?

Mr. LAFFERTY: I have no evidence.

Mr. LIND: That is what you said this afternoon.

Mr. LAFFERTY: No, I merely stated what took place. I have no evidence as to whether it was sponsored or not. All I said was that he was a senior director of one of the major banks.

The views that I hold are not held by me alone. If you were to extend yourselves into the financial community at my age group you would find many who have the same views, but they are not in a position to express them without having economic retaliation taken against them. I say that without equivocation and I am fairly well exposed, as I have already said before, to the financial community.

Mr. LIND: Mr. Lafferty, you also mentioned in your brief that you do not seriously suggest that it is the influence of the banking committee that has prohibited membership of a certain race on the stock exchanges in Toronto and Montreal?

The CHAIRMAN: Perhaps we should deal with that issue separately. Right now we are—

Mr. LIND: We were talking about discrimination and influence.

The CHAIRMAN: Well, perhaps it is an area that, as Chairman, I thought would be related in some way to the question of foreign banks. Perhaps we can get to that part of the brief separately. We are almost finished with the addendum.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): May I ask Mr. Lafferty a question? Again on this question of Bell Telephone of which he spoke and which

he described as a case of discrimination, was that discrimination on the part of the bank or on the part of the Bell Telephone Company?

Mr. LAFFERTY: A combination of the two. Discrimination on the part of the Bell Telephone Company in that they only selected one with whom to make the arrangements without checking competitive rates, and on the group who received the issue they only selected some dealers to participate with them in the distribution and not others. This goes into provincial Ontario Hydro issues and all sorts of things.

Mr. McLEAN (*Charlotte*): Mr. Lafferty, what should they have done? What should the Bell Telephone Company have done?

Mr. LAFFERTY: Normally they would need money in the capital market; say the amount is \$30 million or \$40 million, whatever it may be, it becomes known in the financial community. They invite syndicates to bid and syndicates form themselves together as to what they will bid. The Bell Telephone then takes the lowest bid and the syndicate is permitted to buy in that issue, and then there is the matter of distributing it.

Mr. McLEAN (*Charlotte*): It was a pretty big syndicate, was it not, that took over the Bell issue?

Mr. LAFFERTY: It does not need to be for the size of that issue.

Mr. McLEAN (*Charlotte*): Maybe there was no room for two syndicates.

Mr. LAFFERTY: This competitive bidding, if you take—

Mr. McLEAN (*Charlotte*): If you have not got two syndicates how can you have competitive bidding?

Mr. LAFFERTY: Oh, you have three or four.

Mr. MORE (*Regina City*): Is it not a fact, Mr. Lafferty, that some business people find that dealing with a corporation of their choice serves them better than dealing on a bid basis, and do not some municipal governments and others practice this because they have found that the service they get and the resulting relationship makes it worth while to do this?

Mr. LAFFERTY: It is the same principle where you let a construction contract on a bid basis or where you give it to your particular favourite contractor. The same principle is involved whether the public interest is protected or not.

The CHAIRMAN: Are there any further questions on foreign banks? If not, I suggest we move on to paragraph 6. Any questions or comments on the proposal in paragraph 6 on page 7?

Mr. CLERMONT: Mr. Chairman, according to this brief, Mr. Lafferty would like the Canadian government or some agency to give an explanation to the public for the merger of the Canadian Bank of Commerce with the Imperial Bank of Canada. This is at the bottom of page 7.

The CHAIRMAN: Perhaps Mr. Fulton, or someone, might enlighten me, at least. Were there questions asked in the House about this when it was announced?

Mr. LAMBERT: A statement was made by the Minister of Finance of the day.

Mr. CLERMONT: The reason for my question is that Mr. Lafferty earlier in this brief claims that a group should not go to parliament to obtain a charter. Is this right?

Mr. LAFFERTY: I expressed the view that to my way of thinking it was not a desirable approach.

Mr. CLERMONT: Do you not think, Mr. Lafferty, if the law had been such that to effect a merger they would have been obliged to go to parliament that the public would have been better informed?

Mr. LAFFERTY: No, I think there should be anti-trust and anti-combines legislation which would have established it was detrimental to the public interest to merge the two banks. If such legislation had existed that would have been adequate.

Mr. LAMBERT: But on the other hand, Mr. Chairman, is it not a fact that the legislation as it now stands, and as it stood at the time, requires that any merger of this kind can only take place with the approval of the Minister of Finance?

Mr. FULTON: This is Treasury Board, approved by the cabinet.

The CHAIRMAN: You would say in advance that the judgment of the court, if we had laws dealing with this type of merger in our complex of anti-trust legislation, would automatically have been against it?

Mr. LAFFERTY: If it deprived or impaired the competitive development of the market place the judgment would have been against it.

Mr. FULTON: You know that we took two merger cases to court, do you not, Mr. Lafferty, and lost both of them. These were the first two merger cases that have been taken to court in Canada.

Mr. LAFFERTY: Mr. Fulton, my whole context this afternoon and this evening has been that our anti-trust and anti-combines legislation is insufficient to permit the public assistance.

Mr. FULTON: Well, the courts held that there was not sufficient interference with competition in those two cases. There was still effective competition.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Mr. Lafferty, you speak about strengthening this section 138. Would you consider it a prima facie case of collusion if it appeared that two or more banks were giving the same rate of interest on deposits and charging the same interest rates on loans?

Mr. LAFFERTY: Not at one particular period. It could be a normal adjustment in the market place. The market place would normally adjust. If they changed their prices together at the same time or if they acted together to achieve a certain condition, yes, but not if they happened to have the same rates at the same time, because this is a natural phenomenon and it is bound to take place at some stage.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Is it inconceivable that each bank might reach the same conclusion as to the logical rate of interest, say, even on deposits or to charge on loans? Is it a practical thing to suggest? Personally I think clause 138 is a piece of nonsense. I do not think it will have any effect. I said so at the time it came up and I do not see how you can make it



effective unless you are going to put all banks into proper monastics cells and not allow them to communicate with each other, which means that you are bound to find that the same kinds of institutions operating in the same field at any particular time are going to come up with the same answer.

Mr. LAFFERTY: This is not always true, Mr. Cameron, because if you take the near-bank field of the trust companies you will find for periods of weeks trust companies are offering different rates on deposit; some 4 per cent some  $4\frac{1}{4}$  per cent and some  $4\frac{1}{2}$  per cent, and also offering different conveniences with those deposits.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I am not a lawyer but I would certainly hate to try and prosecute the banks. Fortunately, I am sure they would get off!

Mr. LAFFERTY: One bank which sought more funds might go out and invest in the marketplace, as they do in the short term money market. They bid against each other at very different rates and take funds on term deposit for 30, 45 or 60 days and the highest bidder normally takes the funds.

Mr. LAFLAMME: Do you think it is a bad thing for the banks to have an association?

Mr. LAFFERTY: Yes, I think it is a bad thing to have an association to provide the framework on which they will conduct their businesses. I see that the Inspector General has referred to the Canadian Bankers Association as an educational organization. I have no evidence to the contrary but I think from a general consensus of the financial community that it is not. It is a much more organized unit.

Mr. LAFLAMME: Let us say, for instance, in Montreal that one bank decides to pay, let us say, 6 per cent interest on deposits and the other banks say no, we will not, then they must attract deposits?

Mr. LAFFERTY: I think it is highly undesirable. They have general managers in the Canadian Bankers Association, they are not an educational institution, they have better things to do than run an educational institution.

Mr. MORE (*Regina City*): Would you recommend that it be abolished?

Mr. LAFFERTY: I would.

The CHAIRMAN: It is true that when the Inspector General of Banks said it was an educational institution—and while the record may not show this—he seemed to have a fixed smile on his face but, at the same time, it is my understanding, and I could be wrong, that they do, in fact, offer courses to banks' staffs and have people who—

Mr. LAFFERTY: That is fine. Their personnel managers get together and run the institution with this sort of staff, but then it certainly does not require a general managers' policy to operate it.

The CHAIRMAN: If there are no further questions on Mr. Lafferty's proposals regarding clause 138, before we deal—

Mr. MORE (*Regina City*): Mr. Chairman, just before you move on, Mr. Lafferty makes this statement in his brief:

The banks have literally acted as an avenue through which certain private interests have exploited millions of dollars of the Canadian public's money.

The CHAIRMAN: Where is that Mr. More?

Mr. MORE (*Regina City*): Page 7, the second paragraph. It is an assertion.

Mr. LAFFERTY: Would you like to study this document, the history of this company, the Argus Corporation, the interlocking relationship they had on financial institutions when they put it together? The equity capital of the shareholders appears at the bottom. Let me just read this equity capital for you, it is very interesting.

Mr. FULTON: Would you first relate it to the banks?

An hon. MEMBER: Yes, that is what I would like.

Mr. LAFFERTY: Their major directors were on different banks and the means by which the original financial distribution of securities was made was through compromise.

Mr. FULTON: Can you prove that?

Mr. LAFFERTY: No, I certainly cannot.

Mr. FULTON: Well then, go ahead.

Mr. McLEAN (*Charlotte*): I thought it was the breweries.

Mr. LAFFERTY: It was found that—

Mr. McLEAN (*Charlotte*): That was E. P. Taylor, was it not?

Mr. LAFFERTY: The common capitalization was \$5,411,000. The total assets, if you take the marketable scale, were \$202 million plus another \$10 million. He would put up a comparatively small investment, which was probably loaned by the banks against the equity, and leave it up for the capitalization of several different preferred stock capitalizations, several secured notes, and in this way you have a pyramid structure.

Mr. McLEAN (*Charlotte*): Does the Argus Corporation actually have control of any company?

Mr. LAFFERTY: Yes. They have effective control of Dominion Stores.

Mr. McLEAN (*Charlotte*): No, they actually have control?

Mr. LAFFERTY: Dominion Stores.

Mr. McLEAN (*Charlotte*): Did they ever have 51 per cent of the shares of any company?

Mr. LAFFERTY: They do not need it. They have effective control, which is sufficient. Canadian Breweries, Dominion Stores, Domtar, Hollinger, Massey-Ferguson, Standard Radio and B.C. Forest Products.

Mr. McLEAN (*Charlotte*): They do not have actual control?

Mr. LAFFERTY: They have effective control. They own effective control.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): E. P. Taylor's man always arrives when B.C. Forest Products is in trouble.

The CHAIRMAN: Mr. Lafferty, in your supplementary brief you have several appendices which, I think it is quite fair for me to say, are testimonials with respect to the views advanced in your brief. Two of them are signed by lawyers, one in western Canada and one in Montreal.

Mr. MORE (*Regina City*): That lets you out.

The CHAIRMAN: Yes, that is right, but I am always happy to receive publications. Mr. Lafferty has increased my general knowledge. I mention that these testimonials are signed by lawyers because I found it rather interesting that this was the case in view of the fact, Mr. Lafferty, on page 4 of your brief you say:

It is a well known fact that a practicing lawyer has neither the time, nor in most cases the knowledge or experience, to effectively judge and direct a nation-wide branch banking system that must necessarily relate to the international monetary and banking affairs of the world.

I am wondering, in view of this comment in your brief, whether you have called on people whom you do not regard as particularly knowledgeable in this field?

Mr. LAFFERTY: No, I do not think so, Mr. Chairman. I think that the preparation of this type of brief by a small group of our nature is an uncommon thing to do in the Canadian financial community and you obviously antagonize all sorts of these larger interests. There are many others who are perhaps on the same level of operations who considered it was rather a critical approach to take.

The CHAIRMAN: Perhaps I did not express myself as clearly as I had intended.

Mr. LAFFERTY: One of the suggestions was that lawyers are not qualified to operate banks. The other was the suggestion that lawyers recognize the collusion and intimidation which takes place in the overall structure as a whole.

The CHAIRMAN: I got the impression that you were suggesting that practicing lawyers do not have the necessary knowledge or experience so that they could—

Mr. LAFFERTY: Not in the banking business.

The CHAIRMAN: Then how could they properly assess your views?

Mr. LAFFERTY: I am not expressing my views on the operation of the individual banks. I am expressing my views on the effect of the dominant interests and the collusion in the over-all market economy as a whole which comes into this.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): A lawyer might have additional expertise, Mr. Chairman.

The CHAIRMAN: That is right.

Mr. MCLEAN (*Charlotte*): Mr. Chairman, we have gone into the monetary affairs of the world once or twice. Every time I go to ask something about the monetary affairs of the world you shut me off.

The CHAIRMAN: No, I just wanted you to hold that aspect off until we had a few moments for a general discussion, because I think our practice has been to deal with the specific topics raised by the witness in order to be courteous



enough to give our major attention to the views he wants to discuss with us. I think at this point Mr. More, indicated he wanted to ask something about a particular paragraph.

Mr. MORE (*Regina City*): I would like to ask Mr. Lafferty if he was serious in suggesting that the bank cartel, as he calls it, has the power and has used this power so that people of certain racial background have been denied membership in the Montreal and Toronto stock exchanges, which is a point he seems to make.

The CHAIRMAN: On what page is that?

Mr. LAFFERTY: I do not think it relates to the stock exchanges.

Mr. MORE (*Regina City*): But you mention the membership. There is one in Toronto and one in Montreal, and that some applicant was blackballed in Montreal. What does this have to do with the banks? It seems to me that you relate it here as evidence of discrimination in the power of the banks.

An hon. MEMBER: What page is that?

The CHAIRMAN: It is the last paragraph on page 24.

Mr. MORE (*Regina City*): Yes, page 24.

Mr. LAFFERTY: It reads:

It is for this same reasoning that the Jews in Canada have been largely excluded by direct restrictive practices from entering the financial community.

The CHAIRMAN: What is your question again, Mr. More?

Mr. MORE (*Regina City*): My question is why is this put in a brief having to do with banking? He talked about the cartel the power and the control. Does he seriously suggest that they exercise this control over the Montreal and Toronto stock exchanges to this effect?

Mr. LAFFERTY: You do not have a racial discrimination, perhaps, as a competitive restriction within the financial community environment as a whole. Again I cannot, without a subpoena or by the evidence of witnesses, trace this through and establish where it originates. It is a set of conditions in Canada in our financial markets that we do not have the Jewish participation that we have in the New York market, the London market, the French market or the Swiss market.

Mr. MORE (*Regina City*): You blame this on the influence of the Canadian chartered banks?

Mr. LAFFERTY: I have related it as a surmise to the over-all cohesiveness or collusion of the dominant interests. If my information is correct, there is—

Mr. McLEAN (*Charlotte*): Is not the head of our whole banking system of the Jewish persuasion?

Mr. LAFFERTY: That, I think, is a Crown Corporation.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I wonder if Mr. Lafferty does know. The fact that people of the ethnic origin of Dr. McLean and myself got there first in Canada is a matter which has interested me for a long time,

and we appear to have usurped the position in Canada that has been occupied by Jewish people in other countries. It is a very notable fact. I do not know myself; I have looked at various lists of bank directors and I have not come across a recognizable Jewish name.

Mr. LAFLAMME: What about Mr. Bronfman, a director of the Bank of Montreal?

An hon. MEMBER: Yes, Mr. Bronfman and Mr. Phillips.

Mr. FULTON: Lazarus Phillips of Montreal.

Mr. LAFFERTY: They are comparatively new. I think Mr. Lazarus Phillips appeared in 1956 and Mr. Bronfman shortly afterwards.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): But they certainly do not play the role in the financial institutions of Canada that they do, for instance, in the United States. I do not know what causes this except, as I say, the people whom I described to Mr. Paton of the Toronto-Dominion who have an ethnic proclivity for getting there first were there before the Jewish people were in Canada. It is quite significant that they do not play an important role. I think you are to be commended for—

Mr. LAFFERTY: They are a highly competitive people and when you have a restricted atmosphere and they cannot operate, then I think you can come to a logical conclusion.

The CHAIRMAN: Mr. Lafferty, is there not presently at least one Jewish member on the Montreal Stock Exchange?

Mr. LAFFERTY: Yes, subsequently to this brief.

Mr. FULTON: Are Lazarus Freres members of the Montreal Stock Exchange?

An hon. MEMBER: It was Lazar Freres.

Mr. LAFFERTY: No, an international banking house.

The CHAIRMAN: Mr. Lafferty, I recall reading that in Montreal two individuals of the Jewish faith applied for positions with a certain firm—

Mr. LAFFERTY: It was our firm.

The CHAIRMAN: It was your firm? They brought charges against your firm under the Quebec Fair Employment Practices Act?

Mr. LAFFERTY: That is correct.

The CHAIRMAN: On the grounds that they were not hired because of discrimination?

Mr. LAFFERTY: That is right.

The CHAIRMAN: That is your firm?

Mr. LAFFERTY: That is correct.

The CHAIRMAN: This case is still before the courts?

Mr. LAFFERTY: Yes. May I amplify this for a minute. The matter is still before the courts. These procedures become quite complex. I was not directly involved in the incident at the time, one of the partners in our firm was and he

related to the two applicants that to his knowledge they would not be eligible as traders on the Montreal Stock Exchange since there had been no Jewish traders. To our knowledge there has never been a Jewish trader on the Montreal Stock Exchange.

The CHAIRMAN: You just said there is a member firm.

Mr. LAFFERTY: As a member firm; it is different. A trader appears on the floor who trades for the ownership of the member firm. In this case one of the principals of this new firm is a Jewish partner, Mr. Shapiro, but he does not trade on the floor, just as I do not trade on the floor for our firm. But you need a trader on the floor who will execute the transactions on the floor of the exchange itself. We were seeking a trader.

The CHAIRMAN: This matter is still before the courts and they have not given their decision?

Mr. LAFFERTY: That is correct.

The CHAIRMAN: Is it also correct that one reason why a decision may not have been given up to now is that one of the defences which was raised was that the Quebec law was ultra vires of the Province of Quebec.

Mr. LAFFERTY: This is correct.

The CHAIRMAN: This is one of the defences raised on your behalf?

Mr. LAFFERTY: Yes, it was not at our suggestion. The matter was taken out of our hands by our lawyers and referred to another firm, which happened to be a Jewish firm. This firm had handled a previous case and they felt that in the previous case they had adopted this position, therefore they had to be consistent and adopt it with ours.

The CHAIRMAN: You do not give instructions to your lawyers?

Mr. LAFFERTY: We are not knowledgeable enough on the legal aspect of this matter. They asked us if we were in agreement with following it—I was not in town at the time—and it seemed a sensible course. They asked me by telephone and I said I would check with our lawyers in the other firm and see if they agree with this. They agreed with it, so I said, "Fine, go right ahead".

They were in a difficult position. They either had to take our case and put it on the basis of the other one which they had sought, or base the defence on this previous case, on this other supposition.

The CHAIRMAN: There is no question at the moment that charge are pending against you that you did not hire these people because of their ethnic origin?

Mr. LAFFERTY: Frankly, I am not quite sure what the position is. There are various arguments which have to be presented by counsel for both parties. These have been deferred at different times by the prosecution. The last date I had was December 16, yet as far as I can ascertain, and I meant to write before I left, our lawyers have not found out.

The CHAIRMAN: Let me get this straight. The charges were laid against your firm, the matter was brought into court and a final decision has not yet been rendered.



Mr. LAFFERTY: It has been brought into court in the sense that it has been filed in court.

Mr. LAMBERT: Why is this subject being—

The CHAIRMAN: That is why, as you may know, I am deliberately not asking—

Mr. LAMBERT: Why pursue it?

The CHAIRMAN: I thought in the light of this paragraph and the questions that have been asked that it might be a useful addition to the record.

Mr. LAFFERTY: Mr. Chairman, I might say—

The CHAIRMAN: My questions only related to what is a matter of public record.

Mr. LAFFERTY: At the particular time this occurred we had two Jewish members on the staff.

The CHAIRMAN: Are there any further questions of our witness at this time?

I would like to thank you, Mr. Lafferty, for—

Mr. CLERMONT: I think Dr. McLean would like to ask a question on—

Mr. McLEAN (*Charlotte*): Well, if we want to go into international affairs. Of course, we do not want to hear it because it is at the bottom of everything.

An hon. MEMBER: Gold reserves?

Mr. McLEAN (*Charlotte*): Certainly it is.

The CHAIRMAN: Mr. Lafferty, we want to thank you for giving us a point of view which has been most stimulating and I think it will assist us in assessing the views put forward by the banking community.

Mr. Howes, would you like to step forward?

Gentlemen, our next witness is Mr. Terry Howes, who has submitted a brief to us and asked for an opportunity to appear. He tells me that he could best be described as a salesman or as an entrepreneur generale. These are his words. I think to save time, as we have had his brief for some days, perhaps we might move directly into questioning. It will be noted that he has made specific recommendations through paragraphs numbered 1 to 17 and has been kind enough to append a number of very interesting articles. I think, therefore, we should proceed with our questioning roughly along the same order that he has made his recommendations to us.

I would ask those who wish to question Mr. Howes to so signify.

Mr. FULTON: Mr. Chairman, are you going to ask Mr. Howes to identify himself?

The CHAIRMAN: It is my practice, Mr. Fulton, before the beginning of the committee meeting to ask the witness for some general information, which I present to the Committee, to assist us in situating the views of the witness in the general complex of our considerations. Mr. Howes said that he is best described as a salesman, and then he added the phrase "entrepreneur general". I must say that that is the limit of the information I have to present to you, which is as a result of a very brief conversation with him between the time we excused our

previous witness and the time I presented him. If other members of the Committee wish to have more information, I am afraid I will have to invite them to question the witness directly.

Mr. FULTON: I wonder if Mr. Howes would care to identify himself further as to his business associations so that I would know his background.

Mr. Terry HOWES: Mr. Fulton, may I say that I make a living, as well as I can, as an entrepreneur. Surely it would not have any bearing on my presentation to this Committee. Let me put it this way: I am not associated in a financial community, as these other gentlemen were who preceded me I do not claim to be as knowledgeable as they are of money markets and all these complicated things.

Mr. FULTON: Are you a member or an officer or a shareholder in an organization called the O.S.C.A., the Ontario Sporting Clubs Alliance?

Mr. HOWES: Yes, Mr. Fulton. Go ahead.

Mr. FULTON: Are you?

Mr. HOWES: Mr. Fulton, this is just said to smear me. You know that, do you not?

Mr. FULTON: Mr. Howes, I am asking you a question.

Mr. HOWES: Carry on. The answer is yes. Gentlemen, it is going to be very interesting to hear this. This was just said to smear me and it has no bearing whatsoever on my suggestions about the banking community. You know that, Mr. Fulton. Carry on.

Mr. FULTON: Are you associated in any way with Sovereign Publishing Company?

Mr. HOWES: Yes, that is correct.

Mr. FULTON: Did you publish something under the heading of "Air Force Diet?"

Mr. HOWES: Yes, we did indeed.

Mr. FULTON: Have those organization been the subject of a United States Federal Post Office Department fraud order?

Mr. HOWES: Right.

Mr. FULTON: Denying you the use of the mails?

Mr. HOWES: Right.

Mr. FULTON: This was as recently as 1965 and 1966?

Mr. HOWES: That is correct.

Mr. FULTON: Were you the advertiser, or associated with the advertiser, of an advertisement headed: "640 Acres of Wildlife—\$20."

Mr. HOWES: The same.

Mr. FULTON: It reads:

For \$20 a year plus \$6 taxes you can lease a 640 acre wildlife domain near the Canadian border. Untamed paradises.

Mr. HOWES: To save a lot of talk I will just give the whole thing to you. carry on; Mr. Fulton.

Mr. FULTON: Well, give us the whole thing, then.

Mr. HOWES: Mr. Fulton, some years ago I decided that the field of shareholders' rights was the one field which was keeping this country from doing as well as it should. Now, I made a considerable study of it and I determined that the banks were the worst offenders respecting shareholders' rights. Now, two years ago the Porter Report came out and it said that as far as these learned gentlemen were concerned no body of shareholders which they could determine was really interested in knowing or cared about the financial affairs of the banks of this country. So, I felt for myself and by myself that I did not think this was the case. I decided that I would try, in a very democratic way, to solicit votes in one of our banks. If I said that they took less than kindly to this, that would be one of the understatements of the century. I have had no peace from that day to this, including from your own good self. But anyway, here I am.

Mr. FULTON: Have you and I had any correspondence?

Mr. HOWES: No, we have not sir. Why should how I make a living be germane to this meeting? Why do you ask that? May I say further that this so-called fraud order that the U.S. Post office has against us would put the Court of the Star Chamber to shame. First of all, we were accused by unnamed accusers, a hearing was held in camera when we could not defend ourselves and we have subsequently been denied the right of appeal. Now, this happened in the United States, not in Canada. I am a Canadian citizen and I am proud to say it. If anyone has anything against me and feels that I have done something wrong, bring it before the Canadian courts, not where I cannot defend myself. Maybe we can continue with what we are here for tonight, now that this matter has been brought up. Is there anything else you would like to know?

I am Canadian born and raised and proud to say it and the father of seven children. I feel there is a real injustice in our banking system. Go ahead.

Mr. FULTON: Were you the subject of an article in *Maclean's* magazine of March 20, 1965?

Mr. HOWES: Indeed I was.

Mr. FULTON: Did you sue them for libel?

Mr. HOWES: Did I sue them for libel? Did they say something libelous?

Mr. FULTON: I am asking whether you sued them for libel?

Mr. HOWES: The answer is no. Carry on.

Mr. FULTON: I think the article speaks for itself. There is just one other question. Are you associated with a group known as the Great Northern Pulp and Paper Group?

Mr. HOWES: Yes, I am.

Mr. FULTON: That is all, Mr. Chairman.

Mr. HOWES: Does this have to go on, Mr. Gray? Really, does it?

The CHAIRMAN: I think at least to some reasonable extent it is useful to know the background of the witness so that we can assess his views in the light of his experience in the business community—



Mr. HOWES: The story is that I used to live a nice, peaceful life until I felt that I should try and see if perhaps the fiction was in fact the fact. I decided that I would solicit a few votes, in a very democratic way, from the shareholders of this bank. Since then, as I say, I have had no peace at all. However let us carry on. We are finished with this now, I hope gentlemen. You have heard about all the dirty linen they can find and this the worst they can find out about me. Go ahead.

Mr. McLEAN (*Charlotte*): I do not understand about soliciting proxies.

Mr. HOWES: This is the way the fiction works. Let us go away back in history. Years and years ago when limited companies were first formed they were collections of partners who were truly democratic people. They would be sitting like we are sitting here tonight and they would truly have to report to their partners. Then they came to be shareholders and they still would have to report, but gradually shares became more and more widely held until where today, most assuredly in the banks, as Mr. Lafferty said,—I do not agree with everything Mr. Lafferty said but I certainly do here—it is just a complete and absolute mockery. If you dare say one single word you will have no peace at all. They do have terrible powers.

Mr. McLEAN (*Charlotte*): It does not come from the shareholders. Who does this “no peace” come from?

Mr. HOWES: It comes from the management of this particular bank. Or, in this case, from their public relations outfit, whom I am sure are represented here tonight.

The CHAIRMAN: Why would they be against you?

Mr. HOWES: Mr. Gray, I have asked myself this many, many times because I did this in what I thought was a very democratic fashion, I really did, and with no axes to grind against these people. The only answer I can find for you, sir, is that I feel that—and this is what all of us here should be concerned about—they have such fantastic power and there are virtually no checks on balances over them, virtually none. It is like a government running itself without holding an election. That is just how they work.

The CHAIRMAN: What did you try to do that they did not like?

Mr. HOWES: I simply came down here to room so-and-so in the Parliament Buildings, or sent my girl down to do it, and got a list of the shareholders and I wrote them a letter and said, “We feel, in line with the recommendations of the Porter Commission, that considerable changes should be made in the Bank Act”. Now, further to that we said that the management of this bank has made some God-awful goofs and we feel that they should be at least chastised for it.

The CHAIRMAN: When did you send this letter out?

Mr. HOWES: About a year ago. The meeting was the second Tuesday in December, so it was a year ago December.

The CHAIRMAN: I see. When were these fraud orders made?

Mr. HOWES: Slightly prior to that.

The CHAIRMAN: But prior?

Mr. HOWES: Put it this way: It was between when I sent out the letter and when the meeting was held.

Mr. McLEAN (*Charlotte*): What did they do to you?

Mr. HOWES: Who is "they", sir?

Mr. McLEAN (*Charlotte*): The people whom you have this against? I do not understand this—

Mr. HOWES: Mr. McLean, I do not have anything against anybody.

Mr. McLEAN (*Charlotte*): You gathered up some proxies, and you say that since then you have had no peace.

Mr. HOWES: What is that again, sir?

Mr. McLEAN (*Charlotte*): You said that since you have gathered up some proxies you have had no peace.

Mr. HOWES: Yes, that is right.

Mr. McLEAN (*Charlotte*): Who is disturbing your peace?

The CHAIRMAN: Are you suggesting that some banking interest is trying to do something against you because you hold these proxies?

Mr. HOWES: Yes. This bank retains a firm called Public Relations Services, Limited. They have done their best to tell the press, including these gentlemen here, you can rest assured, and including our good friend and colleague, Mr. Fulton—

Mr. FULTON: Do they retain *MacLean's* Magazine, too?

Mr. HOWES: Did *Maclean's* say something bad about me?

Mr. FULTON: It is up to you to judge. Did you not sue them for libel?

Mr. HOWES: It is up to you to produce it.

Mr. FULTON: You have asked me to:

Terrance Howes and John Heaven, two Toronto men in their mid-thirties, don't much resemble the conventional images of buccaneers, except for a certain raffish derision in their eyes when confronting government officials or solid businessmen. Yet in their four-year partnership, they have separated the public from more money than many men ever see, most of it by the sale or rent of Canadian land which they neither own nor want to own.

These are not my statements, and I ask if you sued *Maclean's* Magazine for libel when those statements appeared.

This relates to O.F.D.A.

Mr. HOWES: Gentlemen, all right; I am a thief; a crook; a no-goodnik from the word "go". Now, if we have finished with that, can we discuss my proposals?

Mr. FULTON: I suggest that we do, Mr. Chairman.

Mr. HOWES: Thanks very much.

The CHAIRMAN: I think we are in a position to do that, but it is always useful to find the basis which leads a person to make certain proposals; although in

fairness to the witness I think we should be prepared to consider his proposals on their own merit.

Mr. McLEAN (*Charlotte*): Yes; but I would like to know why the proposals are made.

The CHAIRMAN: Yes, that is right.

Mr. HOWES: Because they need to be made, Mr. McLean. Is that a good reason? I think I can convince anybody with an open mind, which I am quite sure you gentlemen have, that they need very much to be made, indeed, and we have once every ten years to do it.

The CHAIRMAN: All right. Let us look at paragraph 1. Are there any questions or comments on the views put forward there?

Mr. LAMBERT: To get down to paragraph 1 on page 5, in what precise respect would you indicate that the annual statements made by the banks should be changed so that, in your own words, they would become more meaningful?

Mr. HOWES: Certainly I am not knowledgeable on bank statements. Very few people in the world are. What I did was to write to this gentleman in New York, who is acknowledged—and I think he probably is—to be one of the experts in the world, and he very kindly sent me along what he thought were the ideal bank statements. I certainly am not knowledgeable on them. I am quite frank here. How many of us are? He is.

Mr. LAMBERT: I notice you have included Mr. Keat's article in the Bankers' Monthly. Presumably you have attended an annual meeting of a bank, I take it?

Mr. HOWES: Yes.

Mr. LAMBERT: And you have put forward some of these proposals, or asked questions with regard to them.

As a shareholder in a bank, if you are asking the management to make their annual statements more meaningful—and here I have some sympathy; I think, generally, in this modern day some of the statements could be amplified and I do not think the banks would object greatly to that—surely you had some idea of what you wanted, without merely cribbing something that someone else has written and advancing it as your own proposal.

Mr. HOWES: If you borrow money at wholesale and loan it at retail it need not be all that complicated in the books.

Mr. LAMBERT: But you made the statement initially, if I may paraphrase your words, that the banks had—"mistreated" is the wrong word—but had not properly treated their shareholders in withholding information from them, and so forth.

Mr. HOWES: Yes, definitely.

Mr. LAMBERT: Essentially those are your words, or the meaning of them.

Mr. HOWES: More or less; but they are fine words.

Mr. LAMBERT: That is generally your meaning. Now, surely you must have a reason, because you say if you make a study you come to this conclusion. You have made this study yourself, presumably, and have made the conclusion. Now, will you enlighten us on what—



Mr. HOWES: Would you feel that a bank's shareholders should know, for example, of a \$2 million loss which, although compared to the bank's capital is not all that money, is in fact a substantial amount of funds? Should they know of this loss? Should it not be brought to their attention at their shareholders' meeting? Suppose you had put up the funds for me to go into business—God forbid that we should see the day! Years go by and things have gone well. In the meantime, there has been a very substantial loss one year. Do you not think that I should tell you about it, as my boss? Would you not think so? Well, this particular bank had a \$2 million loss one year and it was the most stupid thing you ever heard of.

Mr. McLEAN (*Charlotte*): Which year was that?

Mr. HOWES: It was two years ago. They put a \$2 million mortgage on a herd of cows, but they did not ever bother to go and look to see if the cows were there, and they were not. How about that, Mr. Fulton? How would you feel if I—

Mr. LAMBERT: Was that not a case in southern Alberta in which there had been a prosecution, where there were attempts at recovery? I do not know whether it was ever established that there was a loss in the end order?

Mr. HOWES: If they recovered anything at all it would be one of the wonders of the world.

Mr. LAMBERT: Were you able to obtain the information when you went to the shareholders' meeting?

Mr. HOWES: Yes, I was. I have it all here. I brought this up at the shareholders' meeting in a very democratic way and asked the—

Mr. LAMBERT: And you got the answer?

Mr. HOWES: I am trying to think, because I was at three of those meetings. We have a representative here from the Bank of Commerce, who could tell you—this gentleman here.

Mr. LAMBERT: I am interested in knowing if you got the answer.

Mr. HOWES: Now it comes to my mind. I did not.

Mr. LAMBERT: You did not get the answer.

Mr. HOWES: The chairman of the bank did not give me an answer. How about your getting up, and I will—

Mr. LAMBERT: I am not in your position. You are making the assertions, not I.

Mr. HOWES: In the meantime, are you going to answer those questions? Do you think that should be in the financial statement? Do you think it should be in there? I think it should have been, and that is what I said.

Mr. LAMBERT: I am not too sure.

Mr. HOWES: Mr. Scott, the successor to Mr. Elderkin, who might be in the room today, said, according to the *Financial Post* last week, that among the most important checks and balances we have on bank management is the internal audit which I think is a mockery and a farce. We would like to think, as citizens, that they had a very good internal audit. I have always thought they had, too,

really. But if a bank has a \$2 million fidelity loss—the largest ever in this country—do you not think that perhaps it should be brought to the shareholders' attention? I do, and I said so.

Mr. LAMBERT: That is your privilege, as a shareholder. Are you still a shareholder?

Mr. HOWES: Yes, I am.

Mr. LAMBERT: Were there any other points on which you felt that there should be further disclosure?

Mr. HOWES: They are all in this brief here.

Mr. LAMBERT: Yes; but—

Mr. HOWES: And they are all pretty well in the Porter report. I say that I feel we should do this and we should do that, and, what is more, there is a substantial body of the same opinion. I have \$3 million worth of proxies, and they are in this briefcase here. Thirty-thousand odd shares agree with me that these changes should be made.

What I was trying to do, in a very democratic way, was to establish that, in fact, there is a substantial body of shareholders who would like to see the banks' affairs properly set out. I do not agree with all that Mr. Lafferty said—and he did not have to be quite so verbose in saying it—but banks have phenomenal power, and this, gentlemen is the basis of my presentation to you: Should there be this concentration of power in our democracy?

Think about this, gentlemen, because you have seen an example of it tonight in what I am going through. It is something to be frightened about. Yes, have a good laugh.

Mr. LAMBERT: But, surely to goodness, if you were in—

Mr. HOWES: May I finish, sir?

Mr. LAMBERT: If you were a shareholder in another corporation—

Mr. HOWES: We should all be very concerned indeed that in our democracy we have power blocs like this, without democratic checks and balances. And, gentlemen, when you are writing this law, please do not forget it. It is a frightening thing.

Mr. McLEAN (*Charlotte*): I have always been of the opinion that the proof of the pudding was in the eating.

Mr. HOWES: I have done it myself; I did not read about it. I had the guts to do it—and do not think that it did not take a lot of guts.

Mr. McLEAN (*Charlotte*): But what became of the \$2 million? What was it charged to?

Mr. HOWES: How do I know? How can you tell?

Mr. McLEAN (*Charlotte*): Well, why should you not know? You are the man who—

Mr. HOWES: Indeed, why should I not know?

Mr. McLEAN (*Charlotte*): If you can read a balance sheet—

Mr. HOWES: Balance sheet, "shmalance" sheet—nobody can make any sense at all out of them.

Mr. McLEAN (*Charlotte*): They can not?

Mr. HOWES: This gentleman here, Mr. Smythe, is a very knowledgeable and thoughtful scholar. He is a professor at a university in Toronto. His colleague is at Carleton College. They can speak much more knowledgeably than I—and at least I am frank about that. It does not make any sense to me. As a matter of fact, I can not keep my own cheque book straight. And I bank, incidentally, in Buffalo. How do you like that one?

Mr. McLEAN (*Charlotte*): Well, I speak from 50 years of experience—

Mr. HOWES: That is fine, Mr. McLean; grand; that is good. You should know. You tell me where they hid the \$2 million.

Mr. McLEAN (*Charlotte*): I am asking you.

Mr. HOWES: It is your—

Mr. McLEAN (*Charlotte*): I imagine they charged it to inner reserve. I do not know.

The CHAIRMAN: Order, please. Our customary procedure up until now has been to have the members ask the witness questions.

Mr. HOWES: Mr. Chairman, it did not start out very well, you know. I am no saint, either, and I admit it.

Mr. CLERMONT: Mr. Howes has an example of the disclosure of loss. Does it compare, for example, with the action of the management of the First National City Bank which found itself in the embarrassing situation of discovering a huge loss? What do you mean, Mr. Howes, by "huge"?

Mr. HOWES: It was eleven odd million dollars.

Mr. CLERMONT: How much?

Mr. HOWES: Eleven odd million dollars.

Mr. CLERMONT: I thought we were told by a previous witness that it was about \$4 million. This is the First National City—

Mr. HOWES: According to this it was \$11 million. I do not know, Mr. Clermont. It was a very substantial loss.

Mr. CLERMONT: I will accept "substantial loss", but—

Mr. HOWES: What has First National City got to do with it, anyway? We are on paragraph number 1 here.

Mr. CLERMONT: Yes, we are on number 1; but it is about loss disclosure.

Mr. HOWES: I see. Well, from my recollection it was \$11 million. I am just going by press reports.

Mr. CLERMONT: That is what I wanted to find out.

Mr. HOWES: I am sorry, Mr. Clermont. I did not mean to be rude to you, sir.

Mr. CLERMONT: That is all right. I can take it and give it back.

The CHAIRMAN: Are there any further questions on paragraph 1?



Mr. HOWES: Gentlemen, there is just one thing further that I have to say. Since this was sent here, on November 30, our good friends, the Bank of Commerce—fine folks that they are—they are 49 per cent owners of a firm called United Dominions Corporation of Canada Limited, and subsidiary companies, a very substantial firm. Now, a big point made by the Bankers' Association is that it would be bad for public confidence to disclose all these things which we feel need to be disclosed. They make a really big deal of this. Let us say that it may be that they speak with forked tongues.

On December 13, which was, just nicely, two weeks after everybody had to have their briefs in, United Dominions Corporation of Canada Limited and subsidiary companies, due to the realities of the financial marketplace, as Mr. Lafferty says, could not sell their debentures unless they came up with the goods. They just could not do it. The goods they came up with—and here it is; the whole works—and if this is the case the fact is the exact opposite—

The CHAIRMAN: You are referring to the statement entered by the United Dominions Corporation?

Mr. HOWES: That is right. I would like you gentlemen to have a look at this. I am sure that our good banking friends would give them all they wanted. It is the whole "works".

The CHAIRMAN: You are suggesting that there is more information in this statement of a subsidiary—

Mr. HOWES: Have a look at it.

The CHAIRMAN: —which issues debentures, than in the statements of the parent bank.

Mr. HOWES: Yes, if you would like to know from the liquidity statements of September 30 exactly how much funds they have got out, how much is in trucks and how much is in different markets, the whole "works" is here.

Now, here is the thing: the fact of the matter is that instead of its being bad for public confidence that people should know, just ask yourselves this: What is it that, if the public knew about it, would ruin their confidence in the banks? These good gentlemen from the Bankers' Association are coming here again; am I correct? Ask them this question: What is it that, if disclosed, would cause the public to lose confidence in our banks? The answer would be a very fascinating thing to hear.

The CHAIRMAN: I think we have asked them that already.

Mr. HOWES: Well, maybe you should ask them again in the light of what you see here, because when the market actually does go "lousy" for funds, which is, as Mr. what's-his-name said, absolutely "grim"—those Hartford insurance companies will not loan Canadian companies 10 cents. And who can blame them? Would you gentlemen lend them any money? I certainly would not even if I had any money to lend.

The CHAIRMAN: But you have it in Buffalo.

Mr. HOWES: Yes, I do; what little funds I have are in Buffalo. Do you know why? Because they do not charge for clearing cheques in Buffalo.

Anyway, there is the whole "works" from our good friends and colleagues, the Bank of Commerce.

What is that, Mr. Fulton, I did not hear you?

Mr. CLERMONT: How can the banks be our colleagues?

Mr. HOWES: Well, we will say our "countrymen". Okay?

Mr. LAMBERT: All right; but since you are showing expertise in interpreting the financial statements of this particular corporation—

Mr. HOWES: Can I speak to this learned gentleman, here? It is better to work in a man's language. Even a "nut" like me can understand it.

Mr. LAMBERT: Yes; but, on the other hand, you told us at the beginning that you could not understand, or make heads or tails of, any financial statements. I asked you, Mr. Howes, in all sincerity, a shareholder of a chartered bank, and having attended meetings, how you felt that the statements were not very meaningful, and you said, "How do I know? How can I understand them?"

Mr. HOWES: They are gibberish.

Mr. LAMBERT: Then you come along with something else, a series of financial statements, and say, "Look at how well they are prepared".

Mr. HOWES: If you are finished talking, sir, I would like—

Mr. LAMBERT: You have suddenly acquired knowledge if you were able to qualify these as meaningful to you, and as being properly prepared; yet a few moments ago you told me that you could not tell me how and why statements should be meaningful. I am trying to get you to help us.

Mr. HOWES: You forgot the key word, sir—"bank" statements; and I should say, further, "Canadian bank statements."

Mr. LAMBERT: I asked you how they were not meaningful, and how you wanted to make them meaningful, and you said that you did not know anything about financial statements.

Mr. HOWES: I think it is a little out of sequence, but at any rate—

The CHAIRMAN: Well, I think, perhaps, Mr. Howes made the suggestion that they should give greater information on their losses.

Mr. LAMBERT: This will appear in his brief.

The CHAIRMAN: Yes; and, secondly, he has made some specific proposals in general terms—whatever their source—which I would gather he supports, and he is putting them before us for our consideration. That is basically it.

Mr. HOWES: What I have done, Mr. Chairman, is to dig up what are acknowledged, at least in the American banking community—and I hesitate to say it, because I am pariah in the Canadian banking community—to be the experts. They were kind enough to send along, without any charge, what they thought was the ideal statement. When I say, quite frankly, that I am not knowledgeable I am just admitting my ignorance.

The CHAIRMAN: But you are submitting—

Mr. HOWES: Well, I am saying that these are the experts.

The CHAIRMAN: Yes; you are submitting to us, with your commendation, actually, the articles and so on, written by individuals, which are appended to your brief.

Mr. HOWES: Yes; for your consideration.

The CHAIRMAN: Yes. I think that in fairness to Mr. Howes we should take what he is putting forward in the spirit in which he is doing it.

Mr. LAMBERT: Well, I hope so.

The CHAIRMAN: Yes.

Mr. HOWES: Thank you, sir. May I, by the way, gentlemen, bring another matter to your kind attention? It is very—

The CHAIRMAN: Well, it is true that—

Mr. HOWES: This is not what we were discussing, sir.

The CHAIRMAN: Order, please. Although I did permit certain questions to illustrate the background and circumstances which led to your making these presentations to us, as we have done with other witnesses, our general procedure is to deal in as orderly a fashion as possible with the specific points raised by the witness. You have been good enough to make your points in quite an orderly fashion, numbered 1 to 17, and have even given us a bit of poetry to cheer us on our way, as a conclusion.

Mr. HOWES: Well, humour does not do any harm, does it?

The CHAIRMAN: No; not even around the Finance Committee. We have to try—although it is not always easy—to proceed in this order.

Your first point is to urge that annual returns should be complete in every respect. You have submitted, in support of this, an article by Vincent Egan, who, I gather, is of the *Toronto Star*, and so on.

Now, are there further questions on paragraph 1?

Mr. HOWES: Could I add a little something?

The CHAIRMAN: Well, our time is limited, and there may be questions on the other paragraphs.

Mr. HOWES: It will just take one second; really it would. These gentlemen here would like to hear it.

The CHAIRMAN: You have checked with them, have you?

Mr. HOWES: Well, they are my friends; I am sure they would like to hear it. Standard and Poor, who do the rating of people all over the world—or in North America, at any rate—do not rate our banks. Do you know why? They say it is because they cannot get any information and they do not know what is going on. The largest brokerage firm in the world says: The reported net income of the individual bank does not reflect full earnings power, since it is stated only after reserve, after transfers of undisclosed amounts to or from inner reserves. Inner reserves represent funds set aside as additional security against possible future liabilities; these reserves are partially tax-free. Although internal reserves then are not available for individual banks, transfers to inner reserves are reported for the system as a whole—and it goes on.

In other words, you cannot tell “beans” about them—not a thing.

The CHAIRMAN: Although you did not want to give the name, I think, perhaps, unless this is marked as confidential, that we should know who this is.

Mr. HOWES: It is Merrill, Lynch, Pierce, Fenner, and—



The CHAIRMAN: Yes; copyright 1964, Merrill, Lynch, Pierce, Fenner, & Smith, headed "Canadian Chartered Banks". That is what you quoted from?

Mr. HOWES: Yes, sir.

Mr. McLEAN (*Charlotte*): Well, you can tell what they bring out of inner reserves by the income tax they pay, can you not?

Mr. HOWES: There are reserves before and after taxes. There is something called a rest account. You know, that account never gets a rest. If they lose too many bucks on a herd of cows they move it out of the rest account. It is the biggest farce.

Mr. McLEAN (*Charlotte*): There was a fellow who looked at them coming around and he eventually made good and became a millionaire; so it works both ways.

Mr. HOWES: What I have to ask myself, and what I think all present should ask themselves, is: How did we get this thing hoisted on us? It is an absolute farce and mockery—this so-called financial statement.

The CHAIRMAN: Are there any further questions or comments specifically related to paragraph 1? Mr. Laflamme?

Mr. LAFLAMME: It is stated in the brief—the pages are not numbered—that the Bank of Montreal, for instance, has more than 24,000 shareholders 22,544 having under 500 shares; 845 having between 500 and 1,000 shares; and 710 having over 1,000 each. Do you mean to say out of all those people none of them knows what is going on in the Bank of Montreal?

Mr. HOWES: Well, we all get these financial statements, for what they are worth, Mr. Laflamme. But suppose you were a shareholder in the Bank of Montreal and you felt that for one reason or another the present management was not attending to its duties properly. You might want to get in touch with your fellow shareholders to acquaint them with a certain situation and to ask—and surely there is nothing wrong, in this fair land of ours, with asking—to be given their vote. You say, "Will you give me your vote! ". You do it every couple of years, do you not?

Mr. LAFLAMME: I am not talking about elections.

Mr. HOWES: Well, it is the same. At any rate, to answer your question: Yes, they would know what is going on because they are mailed the annual reports, for what they are worth. But let us suppose that the shareholders would like to get in touch with each other. In your constituency people just go and knock on each other's doors, but you cannot do that as a bank shareholder. You can only communicate with people with 500 or more shares, and that means \$30,000 odd invested, which is a considerable amount of money. The great bulk of the shareholders are not known and you cannot get in touch with them.

Mr. LAFLAMME: Well, let us talk about the Bank of Montreal again.

Mr. HOWES: Very well, sir.

Mr. LAFLAMME: Who knows what is going on, in your opinion among all those shareholders? Who knows what is going on at the Bank of Montreal.

Mr. HOWES: Mr. Laflamme, I—

Mr. LAFLAMME: If the shareholders do not know, who knows? Nobody knows?

Mr. HOWES: Well, the management knows.

Mr. LAFLAMME: Nobody knows.

Mr. HOWES: If the shareholders have to go by the financial statement they get once a year, then they most assuredly do not know what is going on. Does that answer your question?

Mr. LAFLAMME: I understood it.

The CHAIRMAN: Do you have any questions on paragraph 2?

Mr. LAMBERT: What do you think the effect of that accumulative voting would be?

Mr. HOWES: Well, if you gentlemen, in your wisdom, see your way clear to recommending that our shareholders be able to communicate with each other—and I surely hope I can convince you that that badly needs doing—it means that they may be able to elect their own directors. The way it is now, the sale of 10 million shares—it is really something to behold, gentlemen, this great heap of proxies on the table. I am sure you know how accumulative voting works. There are 70 directors, say; well, instead of voting once 70 times, your one vote has the weight of 70 votes; so that the minority shareholders can get themselves representation on the board of directors. That is what it would do.

Mr. McLEAN (*Charlotte*): One director?

Mr. HOWES: Yes, sir. Is that not better than it is now?

Mr. McLEAN (*Charlotte*): Well, who would this director represent?

Mr. HOWES: Well, he would represent the small shareholders, presumably, if they are ever got together.

Mr. McLEAN (*Charlotte*): The small shareholders, yes; but what small shareholders?

Mr. HOWES: Which ones?

Mr. McLEAN (*Charlotte*): Are the small shareholders all going to get together and elect a director?

Mr. HOWES: Well, if you let me go along further with my humble recommendations I think that will answer itself.

Mr. McLEAN (*Charlotte*): Who is going to get them together? Would it be you?

Mr. HOWES: Supposing something is going wrong in the bank—

An hon. MEMBER: And they did get together.

Mr. HOWES: Well, when this night is over—please God!—I am out of the banking business; so let it be some body else. But suppose it is going so “lousy” and they pull off some more of these huge “goofs”—and they have been pulling some “dandies”—and this is not ancient history, like the Billie Sol Estes deal, you know, which does not make them smell any too good—but at any rate—

The CHAIRMAN: Are you suggesting that Canadian banks are involved with Billie Sol Estes?

Mr. HOWES: Yes.

The CHAIRMAN: Canadian banks?

Mr. HOWES: Sure; unfortunately, this is a photocopy of a photocopy, but I have the first photocopy here.

The CHAIRMAN: How does that fit in with the best evidence rule?

Mr. HOWES: It is like a bump on a log. Anyhow, it is in here, Mr. Gray. I will get it for you.

I am sorry; I am getting a little mixed up. Shall we carry on, gentlemen? Who asked that question?

The CHAIRMAN: I did.

Mr. HOWES: Oh, I am sorry, sir. Was it about Sol Estes and the Canadian banks?

The CHAIRMAN: I asked if you were suggesting that Canadian banks were involved with Billie Sol Estes, which is rather intriguing, if not fascinating.

Mr. HOWES: I was fascinated myself; that is why I brought it up.

We have one of our good representatives from the Bank of Montreal here, and they were the biggest losers, so he should be able to tell you about it.

Mr. FULTON: It is on page 11—

Mr. HOWES: Page 6.

Mr. FULTON: Page VI.

Mr. HOWES: Unfortunately, it is not readable, gentlemen, but I did not mean it that way. Oh, here we are. It has to do with Pioneer Finance in Detroit the underlined part.

The CHAIRMAN: This very quickly gives you the link between Pioneer Finance and Billie Sol Estes.

Mr. HOWES: Our Canadian banks were amongst the biggest lenders to a firm called Pioneer Finance in Detroit. For example, the Bank of Montreal, King Street, \$3,500,000; our good and true friends, the Bank of Commerce, 3 million; the Bank of Nova Scotia, 2 million. Just what they are doing lending money to these American firms when we are supposedly short of funds is beyond me. At any rate, ask them that one, too.

Mr. CLERMONT: Is it because of that that you went to Buffalo?

Mr. HOWES: No.

Mr. McLEAN (*Charlotte*): Was it Canadian money or American money that they lent these firms?

Mr. HOWES: Well, I should imagine it was American money; it was a Detroit outfit.

Mr. McLEAN (*Charlotte*): Was it money, I mean, that they got in the United States, or was it Canadian money, got up here and transferred to the United States?

Mr. HOWES: I am sure I cannot answer that, Mr. McLean; I do not know. Wherever they got it, they threw it away. At any rate, this Pioneer Finance



loaned its money to Billie Sol Estes and his colleagues, then he stole it. What more can you say than that? I do not know if they will get anything back from it or not; I hope they do.

The CHAIRMAN: Oh, yes; I see. In your opinion. The link is there because the Canadian banks loaned money to Pioneer Finance which, in turn, went broke.

Mr. McLEAN (*Charlotte*): They have written this money off in their statements?

Mr. HOWES: How would I know that, Mr. McLean?

The CHAIRMAN: Are there any further questions on paragraph 3?

Mr. HOWES: There have not been any questions at all.

The CHAIRMAN: It is the privilege of the members to decide whether or not they are going to ask any questions. It is one of the elementary rules that we have here.

Mr. HOWES: I hope that means they are for it.

The CHAIRMAN: Well, it is up to them to make up their minds at the appropriate time.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): I cannot understand this section 3, Mr. Howes. Is this a practice that exists in Canada or is this a practice that exists in the United States?

Mr. HOWES: Oh, very definitely in Canada; It is the custom here. First of all, Canadian shareholders are unfortunately—there is nothing that I say to you sir that I cannot document with what I have got in here. Unlike my former colleague, but at any rate—

The CHAIRMAN: Your former colleague?

Mr. HOWES: Well, my predecessor here.

An hon. MEMBER: Are you associated with him?

Mr. HOWES: Shall I say colleague or predecessor?

Mr. LAMBERT: Is it the practice in Canada for brokers to vote stock check which they hold in street form?

Mr. HOWES: Not only that but they make a practice of soliciting the proxies from the brokers; and these are not the beneficial owners of this stock, and it should not be the case.

Mr. LAMBERT: The banks solicit the proxies from the brokers?

Mr. HOWES: I cannot necessarily say, in all fairness and truth, the banks, because I do not know. I know what is done by other corporations; and at any rate it should not be able to be done, in my opinion. They should pass along those proxies to the beneficial owners, for them to decide whether or not they should vote them. Whether the banks do, or do not, I do not know.

Mr. LAMBERT: In Canada do the brokers actually hold back the proxies, do they act on the proxies themselves, or do they pass them on to the beneficial owners?

Mr. HOWES: No, they do not pass them on.

Mr. LAMBERT: This is known for a fact?

Mr. HOWES: Yes, sir.

Mr. LAMBERT: That is your testimony.

The CHAIRMAN: If there are no further questions on paragraph 3, we will move on to paragraph 4.

If there are no questions or comments about paragraph 4, we will move on to paragraph 5. If there are no questions on paragraph 5 we will move on to paragraph 6.

Mr. FULTON: I think that paragraph 6 is an interesting enough paragraph. I am not quite sure that the conclusions in it are warranted.

Have you had any opportunity really to inspect the share register of the Bank of Commerce?

Mr. HOWES: No, I did not, Mr. Fulton, because they will not let you. One cannot do it. The only place to do it is here next door. I sent my secretary down to do that very thing.

Mr. FULTON: You say at the top of a page of your brief:

Holders of 500 or more shares are less than 10 per cent of all shareholders.

Do you mean that they hold less than 10 per cent of the shares that remain? Is that what you mean? I think your own figures rather contradict the statement as you have it there.

Mr. HOWES: I did not mean it that way, Mr. Fulton. I mean that if there are a thousand shareholders over 10 per cent of them have less than five hundred shares. In other words, what this does—and this is the only explanation I can possibly find for it—is that it perpetuates management in these banks. Ask yourself this: What possible explanation could there be for this setup? Have you any comments Mr. Fulton?

The CHAIRMAN: Well, I think it is up to Mr. Fulton to decide whether or not he wishes to ask questions, or make comments.

Mr. FULTON: I asked a question, and I have reread it in my question and answer.

Mr. LAMBERT: What would be the purpose, Mr. Howes, of being able to obtain the names of all the shareholders?

Mr. HOWES: Well, suppose one wants to oust management. How does one go about it?

Mr. LAMBERT: Attend the meeting.

Mr. HOWES: What is the purpose of attending a meeting when there are great heaps of proxies this high on the table? You have no chance at all.

The CHAIRMAN: What you are suggesting is—

Mr. LAMBERT: Why would you want to oust management if this is on the basis of some sort of small shareholders' league that is organized?

Mr. HOWES: I mean, why would anybody want to be elected? Perhaps they just want to be.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): Even political managements are sometimes ousted, Mr. Lambert.

Mr. LAMBERT: Well, I would like you to elaborate a little more on that.

Mr. HOWES: Well, why did your opponent want to be elected last election? Maybe he—

Mr. LAMBERT: He thought it out at a meeting on election day.

Mr. HOWES: Well, for whatever reason.

The CHAIRMAN: But at the same time he was able to get the names of all the voters beforehand from the voters list.

Mr. HOWES: Thank you, sir. I appreciate that.

Mr. CAMERON (*Nanaimo-Cowichan-The Islands*): We all of us try to get those names.

Mr. HOWES: Yes; well, try here. And gentlemen, we have spent a half an hour, and it seems fascinating, you will blow a heap of dust off and here are these names—at least those with 500 or more shares—and these will be a year old. For what reason? We live in an age of automation. I mean when they mail out your proxy forms for you to sign in favour of management, it is done on a beautiful mailing machine, and the whole 24 thousand, I am sure, just go out like mad; but if you want to find out the shareholder—oh, oh.

The CHAIRMAN: What you are saying is that the existing management has access to each individual name, but the shareholder does not?

Mr. HOWES: Sure.

The CHAIRMAN: Can you tell us how that compares with, say, the Canada Corporations Act, or the Ontario—

Mr. HOWES: I tell you, Mr. Gray; these acts—and thank God for it too—are in the process of being changed. I will put it this way: The only companies which make full disclosure—and this is in my brief, too—are ones that are listed on the New York stock exchange. These recommendations are nothing revolutionary gentlemen; I mean these are presently available to the shareholders of companies listed on the big board in New York. Suppose they wish to circularise the shareholders—providing of course, it has to do with the company's affairs—they must put your mailing piece in with their proxy solicitations. You have to pay for the mailing and handling, which is fair enough. Remember, they use company funds; you use your own funds; but at least you can do it.

Mr. McLEAN (*Charlotte*): Ordinarily you can get the share list in an ordinary corporation from a trust company, can you not, by paying so much?

Mr. HOWES: You can go and copy it down. You cannot do it for the banks.

What they have is a list of daily transfers, and what good that is to anybody, I do not know. They have this list of daily transfers and they keep it at their different transfer offices across the world. But if you wish to find out the actual shareholders of the bank you must come here to the Parliament Buildings and dig in these great, big, old tomes and copy them out. Then you get only less than 10 per cent of all shareholders—we will get to this in paragraph number 7 here—and tens of thousands of them are registered in the bank's nonimee names. I am ahead of myself, but that is another interesting point.



Mr. McLEAN (*Charlotte*): Do you mean to tell me that the bank owns its own shares?

Mr. HOWES: Yes sir. The banks have nominees called Roycan, Montor, Bankmont, Gee & Company, and many others. These are owned by the banks.

Mr. McLEAN (*Charlotte*): How do you know that?

Mr. HOWES: Well, the banks admit it, for one thing. All the brokers know it. Whenever the Bank of Commerce buys a share it is made out to Gee & Company.

Mr. McLEAN (*Charlotte*): Yes, they own company shares, I know; but do they own their own shares.

Mr. HOWES: Yes, sir.

Mr. McLEAN (*Charlotte*): What?

Mr. HOWES: Yes, sir.

Mr. McLEAN (*Charlotte*): They own their own shares.

Mr. FULTON: Who is "they"—the directors of the bank?

Mr. HOWES: The banks themselves, sir. The fact is that I happen to be a little more knowledgeable on the Bank of Commerce than on others—not, by the way, out of respect for them; it does not mean that they are any better or any worse than any other bank; but they happen to be the closest one to me. There is no other reason.

Mr. McLEAN (*Charlotte*): Well, if they own their own shares they can vote themselves in, or vote themselves out.

Mr. HOWES: Yes; but they do not own all that number of their own shares. When we get to paragraph number 7—I do not think we are up to it yet—

An hon. MEMBER: I think we are.

Mr. HOWES: Are we? Well, they are forbidden by law to own their own shares. That is what the present act says. However, there are tens of thousands, and probably hundreds of thousands—I do not know, because I got bored looking—but they are right there for anybody to look at—shares in the names of these banks' nominees. Now, who owns them? The bank themselves?

Mr. FULTON: Did you ask the Inspector General?

Mr. McLEAN (*Charlotte*): But you have said that the banks own them.

Mr. HOWES: Put it this way: Suppose you had a private company called McLean & Company or Mac Incorporated. If you were known to be the owner of that company would it not pretty well follow that you would own the shares? If you have shareholders—

Mr. McLEAN (*Charlotte*): I do not know; but if it was against the law I would be careful.

Mr. HOWES: Well, it is against the law. However, there is nobody who is empowered to go behind this facade and find out who, in fact, are the beneficial owners. This is my point. Why have something in the law if there is no way to check on it? I hope you gentlemen will look—

Mr. LAMBERT: Mr. Chairman, I think that perhaps the witness is not aware of this provision in the bank bill, clause 75, subclause (2):

Except as authorized by or under this Act, the bank shall not, directly or indirectly, (c) acquire, deal in or lend money or make advances upon the security of shares of the capital stock of the bank or any other bank;

Mr. HOWES: All right, sir.

Mr. LAMBERT: It says "acquire the shares of the capital stock, directly or indirectly." Now, this is not a new section.

Mr. HOWES: I know; which is why I said that there must be somebody empowered to go behind this facade and see who are the beneficial owners.

The CHAIRMAN: Are you suggesting that the Inspector General of Banks at the present time does not have power to ask for this information?

Mr. HOWES: Oh, no; but from reading the Act can anybody tell me that he has?

Mr. LAMBERT: Now, wait a minute. You are making a flat assertion there.

Mr. MORE (*Regina City*): Mr. Chairman, the witness has named Bankmont & Company and Gee & Company. Are these actual companies that exist?

Mr. HOWES: I suppose I should have gone so far as to go and search in the registry office and see who is the registered owner of Gee & Company. In fact, I did not do it. However, we do not have to look any further than this room. We have a gentleman here from the Bank of Commerce, and he can answer that for you.

Mr. CLERMONT: But he is not on the witness stand. You are the witness.

Mr. HOWES: I will state definitely, for sure and certain—as certain as anyone can be in this world—that shares in the name of Gee & Company belong to the Bank of Commerce.

The CHAIRMAN: Are you talking about Bank of Commerce shares?

Mr. HOWES: Bank of Commerce shares; any shares, but Bank of Commerce shares, as well as others.

The CHAIRMAN: Well those are the ones we would be particularly interested in the light of the prohibition in the Bank Act.

Mr. HOWES: I mean to say, perhaps they are owned on behalf of clients. I do not doubt—as a matter of fact I would be almost sure—that these gentlemen would not contravene a law, but the fact is that, from my reading of the Bank Act, there is nobody empowered to find out whether they are, or are not.

If Mr. Elderkin is here, or Mr. Scott, or anybody from his department, they can answer it, and if I am wrong, well, it would not be for the first time.

Mr. MORE (*Regina City*): Do I understand correctly that you say the Bank of Commerce owns Gee & Co.?

Mr. HOWES: That is right.

Mr. MORE (*Regina City*): That they hold Bank of Commerce shares and you have reason to believe that they themselves are the beneficial owner of those shares.

Mr. HOWES: I do not know that, sir; I have no way of knowing it, but we should be able to find out. It is the only point I am trying to make.

The CHAIRMAN: Are there further questions on paragraph 8?

Mr. GILBERT: To your knowledge, do you know who owns Roycan or Montor.

Mr. HOWES: I do not know.

Mr. GILBERT: Just Gee & Co. Is that it?

Mr. HOWES: Bankmont is obviously the Bank of Montreal.

Mr. McLEAN (*Charlotte*): I think when one of the banks was before us they said Torbay was the Bank of Toronto, the Toronto-Dominion Bank. Did they not say that?

The CHAIRMAN: If I can use the phrase of the witness, we will have our colleague or our friend from the banking industry back with us, and also the Inspector General. It has all been recorded, and we can pursue this.

Mr. FULTON: A lot of directors could go to jail and be subject to very heavy fines, Mr. Chairman, if these allegations are true.

The CHAIRMAN: Yes, that is right.

Mr. HOWES: Really, I do not think it is human affairs. I am sure they would not be so indiscreet; I am quite sure they would not. But the fact is that there is no one in power to find out. Such things have happened in the past; consequently they can happen in the future. Why have a law if there is no way to check on it. I am making a bigger deal here than what this thing amounts to.

Mr. LAMBERT: What makes you think that the Inspector General cannot go behind.

Mr. HOWES: From my reading of that poem you have there.

Mr. FULTON: Clause 139 reads as follows:

Every person who refuses to give evidence under oath or to produce any book or document material thereto when required to do so by the Inspector or his representative when acting under subsection (4) of section 65—

and you have to look at that.

The CHAIRMAN: I think in general the Inspector General has very wide powers to acquire information from banks.

Mr. FULTON: Clause 65 reads in part:

The Inspector, from time to time, but not less frequently than once in each calendar year, shall make or cause to be made, such examination and inquiry into the affairs or business of each bank as he may deem to be necessary or expedient, and for such purposes take charge on the premises of the assets of the bank or any portion thereof, if the need should arise, for the purposes of satisfying himself that the provisions of this Act having reference to the safety of the creditors and shareholders of each such bank are being duly observed and that the bank is in a sound



financial condition, and at the conclusion of each such examination and inquiry shall report thereon to the Minister.

Clause 139 reads:

Every person who refuses to give evidence under oath or to produce any book or document material thereto when required to do so by the Inspector or his representative when acting under subsection (4) of section 65 is guilty of an offence against this Act.

So it is quite clear that the powers of the Inspector to compel complete disclosure are as wide as you would want and some people might say, wider than they should be. Mr. Howes, I think I should record my condemnation of your attitude when you say pointblank, without asking the Inspector, that you are satisfied that all these shares are owned by the banks, when you could have asked the Inspector and conceivably got that information from him, or you could have found out whether he ever had made an inspection to satisfy himself whether or not they were in fact owned by the banks.

Mr. HOWES: Did I say that they were owned by the banks?

Mr. FULTON: It seems to me your brief said so.

Mr. HOWES: If we have to go into it all that deeply, I did not say that. What I said was that I felt that someone should be empowered to make sure.

Mr. FULTON: The Inspector of Banks is empowered to make sure.

Mr. HOWES: That is fine then, Mr. Fulton. I have many mistakes in my life. However, I made them in good faith.

The CHAIRMAN: At least one point in your brief has already found acceptance in the legislative sphere. Are there any further questions on paragraph (8).

Mr. LAMBERT: It could be that the interest on a loan of a certain size is not charged for six months on a demand loan. There is no indication that the interest shall be charged up monthly, quarterly or anything less than annually. Therefore, why should that loan on which for instance no interest is received for six months, be termed a delinquent loan.

Mr. HOWES: I am sure that the people who write the law would write it in a proper legal fashion. What I meant to say was, six months after the due date of the loan; it could well be a one year loan on which no interest or principal was to be paid until one year from that date.

Mr. FULTON: Or the due date.

Mr. HOWES: If there have been no funds six months after the due date.

Mr. LAMBERT: That does not say so with regard to demand loans.

Mr. HOWES: I beg your pardon.

Mr. LAMBERT: And I think today, except for consumer loans, you will find that most Canadian bank loans are demand loans rather than term loans.

The CHAIRMAN: Paragraph 9.

Mr. CLERMONT: Paragraph 9 states:

The Inspector of Banks should be required to supervise closely loans made by banks to finance companies.

Then further on it states:

Apparently the situation was so bad shortly after the collapse, that unless the Bank of Canada had stepped in and arranged that huge amounts of cash be shovelled into many finance companies—

How can the Bank of Canada do that?

Mr. HOWES: Through their re-discount privileges. As Mr. Lafferty was saying—and I think we all have to agree with him here—these things are done by word of mouth. I did not make this up, sir; I have the press clipping here.

Mr. CLERMONT: You say you did not make it up, but you are taking the responsibility for that brief.

The CHAIRMAN: I would wonder, sir, whether the Bank of Canada has the authority to put cash directly from its coffers into—

Mr. HOWES: Arranged. I am not saying it did it. The president of Traders Finance was one who discussed this at great length. Gentlemen, this is not the time to discuss that Atlantic matter but Mr. Lafferty was not kidding; apparently it was really grim.

Mr. CLERMONT: You said that in some ways Mr. Lafferty talked too much.

Mr. HOWES: I did not say that.

The CHAIRMAN: What was said about comparisons?

Mr. HOWES: But anyway, whether or not the Bank of Canada recommended that the banks make funds available—if I must word it in such long legal words—it is my contention that because of Atlantic, British Mortgage and this Prudential thing,—I was incidentally, asked at a creditor's meeting about Prudential Finance—you gentlemen would need no more reason for the Bank Act to be changed than to see those old folks who had been stripped of their funds. It can happen with banks too, you know.

Mr. MORE (*Regina City*): Yes but the Inspector General of Banks, by a regulating and having power over bank loans to Prudential, would not have helped the person who bought their debentures and got stuck. How would that save them?

The CHAIRMAN: I think probably your point there is that it might help the banks, not the—

An hon. MEMBER: It collapsed though earlier.

Mr. HOWES: Maybe that would have been a good thing. But anyway, may I say that I made the recommendation after due consideration, sir. Mr. Saxon in the United States feels the same way, and with good reason. And remember, our American neighbours had much, much tighter banking laws than we have. Maybe we need them.

Mr. CLERMONT: According to your report they had seven bankruptcies in 1966.

Mr. HOWES: Yes sir. Canadian banks are like a cornerstore, you know; they are not all that.

Mr. LIND: Mr. Chairman, mention was made of cash being shovelled into many finance companies.

The CHAIRMAN: Perhaps we should take a moment and help Mr. Howes find his clipping. If you cannot, perhaps you can mail it to us later.

Are there any questions on paragraphs 10 to 15 inclusive.

Mr. MORE (*Regina City*): How would you expect proxies to be recorded if an owner was able to change his proxy up to the time of the actual vote, and with thousands of proxies, how on earth could this possibly work?

Mr. HOWES: The number of shareholders that turn up at a meeting is a small fraction of the total shareholders.

Mr. MORE (*Regina City*): Yes, but how can an owner formally change his proxy up to the time of the vote? If he is not at the meeting he would not have a proxy.

Mr. HOWES: If you have a true election going, there are people of different opinions who solicit one vote. The way it is now—at least in the one bank that I know of—you have to have your proxy in five days prior to the meeting. Things can happen and people change their opinion in that time.

The CHAIRMAN: How do you claim the proxy should be drafted now, sir, with respect to—

Mr. HOWES: The March case, you mean?

The CHAIRMAN: Yes.

Mr. HOWES: Well, you are given the name of the President and two or three of his colleagues, for instance the general manager. You could say: I agree that Mr. so and so, or barring him Mr. such and such, or barring him somebody else can represent me at this meeting. It is such a simple thing. Or you could fill in some other name.

An hon. MEMBER: Do you know his right name?

Mr. FULTON: A little blank space is so easy. It has to be registered surely some time in advance of the meeting, and it takes some time to register.

The CHAIRMAN: Your point is that this blank space is not usually found in the bank proxy forms.

Mr. HOWES: Yes.

The CHAIRMAN: Now on paragraph 16, is it not the custom now that annual reports of the chartered banks be in both French and English.

Mr. HOWES: Well, if it is, I have not seen them. It could well be.

Mr. CLERMONT: Mr. Chairman, I have received an annual report in French from seven banks for 1963, 1964 and 1965. I did not request the eighth one.

The CHAIRMAN: Are there any questions on paragraph 17.

Mr. LAMBERT: Of course, as you should know now, the merger of the Commerce and Imperial was after approval by the cabinet on recommendation of the Treasury Board. Therefore it goes even higher than the Governor of the Bank of Canada. This is a statutory requirement. It has always been.

The CHAIRMAN: We will not ask Mr. Howes to answer questions on his taste in poetry because that is a very personal matter.

If there are no other questions or comments which the members consider urgent at this time with respect to Mr. Howes' submission, I suggest that we



adjourn the meeting until next Thursday. We may want to look at Mr. Howes' brief not only in the light of Mr. Howes himself presenting it, but also in the light of the addenda he has attached and the people who have signed their names to it with respect to the articles and so on.

Thank you, Mr. Howes, for giving us an opportunity to hear your views.

I declare this meeting adjourned until next Thursday at 11.00 a.m.

## APPENDIX "CC"

## POPE &amp; COMPANY, TORONTO 1

Memorandum addressed to the  
Standing Committee on Finance, Trade and Economic Affairs  
in the matter of Bill C-222.

A section of the Bank Act that has received little or no public discussion and yet is far reaching in its effect is section 157. This section was first introduced in the revision that took place in the 1930s. On the face of it, the section would appear to have been inserted merely to forbid an improper use of the word "bank" by unsound institutions wishing to take advantage of the gullibility of the public. In practice, it has brought about greater evils in that by forbidding the use of the words "bank", "banker", or "banking" by those who are not incorporated under the terms of the Bank Act, it has effectively made it impossible for even those foreign banks of the highest repute to offer their services to the Canadian public.

The point that this memorandum wishes to emphasize is that it is not generally realized that the results of this section 157 have been, unwittingly, quite disastrous.

*Firstly:* By using the word "bank" in this manner, Parliament has in effect changed the normal meaning of the word as commonly used in the English language; as an unfortunate legal implication is that any institution carrying on business in Canada and performing banking functions, but not chartered under the Bank Act, is beyond the control of the federal Parliament. This, of course, is quite contrary to the thought of those who drafted the British North America Act.

*Secondly:* As the international banks are, as a consequence of this section, forbidden to open branches in either Montreal or Toronto, our public suffers from a considerable limitation in the banking facilities that are offered to it. This is not necessarily a criticism of the facilities offered by our own chartered banks. As we all know, these rank amongst the soundest in the world. The point is, though, that while they are excellent in their chosen fields, they are somewhat provincial in their approach to international banking. Parliament should not put itself in the position of depriving the public of the more sophisticated banking services that are available in foreign financial centres.

*Thirdly:* This section actually reduces Canada, in matters of international finance, to the status of a third-rate power. It is no exaggeration to say that, financially speaking, the influence of the Canadian dollar abroad is practically nil.

*Fourthly:* The Canadian dollar, because of this section 157, is merely a local currency rather than an international currency.

*Fifthly:* Properly speaking, there is no foreign exchange market in Montreal or Toronto worthy of the name. One grants that the foreign exchange trading departments of the various chartered banks are quite adept at making quotations in American dollars, yet the fact remains that any quotation in Canadian dollars

for any other foreign currency is merely a reflection of the New York market.

*Sixthly:* It is again no exaggeration to say that this section has been responsible over the years for the loss by our exporters of a great deal of business. Manufacturers can well have excellent products for sale, but lacking complete financial advice regarding foreign exchange and foreign credit, they are unable to compete with those who have more financial expertise at their disposal.

It is sheer emotional chauvinism to believe that foreign banks are anxious to come into this country to prey on the savings of our widows and orphans. The finest financial centre in the world is London. In that city there are nearly two hundred branches of foreign banks. The requirements for the starting of a branch of a foreign bank in London are simple. It is merely required that it be licensed by the London Board of Trade, and on its letterhead state the country and year of its incorporation. Contrary to the fears of our chartered banks, a branch of a foreign bank does not deprive local banks of business, but rather brings new business to the financial community.

By the same token sub-section "G" of section 75 of Bill C-222 must be considered iniquitous. It is perfectly proper for Parliament to pass legislation seeing to it that foreign guests behave as good citizens. It is another matter entirely though to propose legislation aimed at causing needless harm to a particular well-behaved foreign guest.

The restrictions imposed on ownership of bank shares by the new section 53 are to be deplored. Sub-section 2 of section 53, which limits the shares of a chartered bank that may be held by one group to 10%, merely serves to perpetuate control by management rather than control by the owners, which is the more proper thing.

Much of the newspaper discussion regarding the revision of the Bank Act has been on the matter of whether or not a limit should exist on the rate of interest that chartered banks may ask for in granting loans. Most of the arguments in favour of retention of the rate ceiling tend to be emotional rather than rational. There are no sound grounds for believing that the chartered banks would take advantage of this new freedom, were it granted to them, by charging rates that could be considered improper. At the present time, the limit is quite unrealistic and produces unhealthy results.

All of which is respectfully submitted,

Joseph Pope.

October 7th, 1966.



APPENDIX "DD"

LAFFERTY, HARWOOD & CO., MONTREAL, CANADA

6 September, 1966.

Memorandum to the  
COMMITTEE ON FINANCE, TRADE & ECONOMIC AFFAIRS  
House of Commons  
Ottawa, Ontario.

In August of last year we submitted to your Committee a brief regarding the proposed decennial revision of the Bank Act. After we had submitted the brief to your Committee we released copies to interested parties with the following letter:

"The Standing Committee of the House of Commons on Finance, Trade and Economic Affairs resolved at their meeting on June 29th, 1965 that the cut-off date for the receipt of briefs relating to Bill C-102 (Decennial Revision of the Bank Act), would be August 31st, 1965. Our brief was filed and acknowledged by this date. It is now, in our opinion, a public document.

"Our submission of a brief to the Committee was prompted by straight forward reasoning.

"We believe the banking, financial and capital markets of a nation must be based on principles that creatively serve the population in all walks of life.

"We believe that in the last 15 years there has been a broad deterioration in Canada in this regard, and that the trend has been towards exploitation rather than creativeness. As a result, we believe our status as a people of self-reliance and integrity as a whole has been weakened.

"We believe it is within our role in the financial community to do what we can to correct this. These are the only motives that lie behind the submission of our brief.

Lafferty, Harwood & Co."

Subsequently, Parliament was dissolved and our brief was never distributed to Committee Members.

A new bill has now been prepared (C-222) and has been referred to your Committee by the House for more thorough examination.

The background thoughts in our original brief are as valid today as they were a year ago. We are therefore resubmitting it to the newly formed Committee of the House of Commons on Finance, Trade and Economic Affairs. We are including in this memorandum some additional observations regarding Bill C-222.

Before discussing certain features of this bill the Committee might be interested in learning of the reaction that we received from different groups in the financial community who had seen our brief.

Most felt that the brief was an open discussion that fairly reflected the views widely held in the sub-surface among financial institutions in Canada.

What is perhaps not broadly recognized is the extent to which the banks dominate the financial community and use this influence to condition the thinking and actions of participants in the community.

Nearly every investment dealer is dependent on a bank for financial accommodation in order to carry his bond inventory. If the banking accommodation is not forthcoming at various critical times in the money and financial markets, then he can be squeezed out of business or severely penalized, and thus the dealers and the major part of the financial community are beholden to the chartered banks. Most of the financial institutions in turn are beholden to the financial community for the services that they provide, and thus there are very few who are in an economic position to isolate themselves from this influence and freely stand on their own feet and express a critical view of the banking system. The general pattern to be found in the financial community is one of fawning response to those to whom the community is beholden. Naturally there is a tendency for the banks to exploit the articulation available to them in furthering their own public image and interests.

Our brief was made available to different members of the financial press, but it received very little news coverage. Excerpts were printed in the *Toronto Star*, but the most extensive articles were published in the *Winnipeg Free Press*, and these were subsequently republished in the *Vancouver Sun*.

It has been intimated to us by the financial press that most financial editors would find it contrary to their interests to publish views reflecting unfavourably on the Canadian banking system.

We have received a number of individual letters commenting on our brief. We have included excerpts from these letters in an appendix to this memorandum.

With respect to Bill C-222 we wish to express the following views. These should be taken in context to the background thinking already discussed in our original brief, which is being submitted to you with this memorandum.

1. Section 25 of the new bill permits the formation of Executive Committees at the board level to act for the directors.

We think this is self-defeating when the intent is to broaden the competitive environment. An executive committee would enable the banks to maintain large boards of directors, the majority of whom are really rubber stamps and whose real service is to strengthen the banks' influence in the social, business and political community. These directors are not for management purposes.

If the formation of an executive committee is permitted there is no incentive on the part of the banks to dismember their present sprawling director structure, which really has octopus connotations. In fact, instead of discouraging its expansion it would permit an encouragement of it.

If a competitive environment were to be achieved amongst the Canadian banks, the present large boards of directors would become too unwieldy to respond to the rapidly changing decisions that have to be made at the policy level of a competitive enterprise. As a result, there would be a natural tendency to shrink the boards to more sensible management proportions in order to

achieve the operating flexibility that would be required. Although the new bill helps to discourage interlocking relationships, there are numerous methods that an ingenious group can devise to circumvent this requirement and at the same time achieve their purpose of exercising a conditioning influence in those areas sought. The banks should of course be seeking to acquire and hold their business on the basis of serving the consumer rather than exercising a pressure through social and business interests, to which the consumer must respond.

2. There are a number of minor technical points which we think should be included in Bill C-222. There are three obvious ones that come to our attention, but we also think that a careful examination should be made to see that the Bank Act conforms to the same principles governing the Canada Corporations Act.

(i) There is nothing in Bill C-222 that requires the banks to disclose to the shareholder the annual compensation paid to the officers and directors of the bank. This is normal and proper practice and is information to which a shareholder is entitled, and we see no reason why the banks should have themselves exempted from this public scrutiny.

(ii) There is nothing in the proposed legislation that would require the banks to report to their shareholders more than once a year. Full and adequate disclosure is now broadly recognized as being an important requirement and contribution to the proper development of orderly capital markets. From the shareholders' viewpoint it is a management responsibility that the owners be kept informed of the progress and operation of their bank. Interim reporting is required under the Canada Corporations Act and there is no good reason why the chartered banks should be exempt from this reporting practice. Most of the major banks in the United States follow this practice. The Canadian banks have made no effort in this regard in the past 10 years, and the reports they have submitted to the shareholders have been a mockery of honest reporting. We think it is time that the banks were required to play a more responsible role in Canadian corporate citizenship. In this historical regard we also think the public auditors have failed to act in the shareholders' interests by the manner in which they have condoned the way the banks have reported their financial affairs to the shareholders in the last 10 years.

(iii) The new Canada Corporations Act and the new securities legislation in the Province of Ontario require that directors and/or officers of the bank report to the Secretary of State or the authorities concerned any insider transaction in shares. There is nothing in the proposed bank legislation covering this, and again we see no reason why the banks should be exempt from this principle of proper disclosure.

3. We are opposed to the concept that the chartered banks should be allowed to issue debentures. The Canadian banks already monopolize a major portion of the savings of the Canadian public. To further extend this monopoly increases the concentration of economic power and denudes other developers' access to the savings that would otherwise be available to them. For the reasons that we outlined earlier, the banks are able to dominate the financial community and thus they would not really be competing in terms of merit in the sale of these debentures with other entrepreneurs.

We think the banks should be encouraged to competitively retain their deposits by effectively serving the consumer and suffer the penalty of loss where they fail to do so.



4. We think Bill C-222 is a step backwards as regards the formation of new banks in Canada. Bill C-102 sought to provide a statutory means by which others in the economy could start a new bank. We believe it should be a statutory right for any group in the Canadian economy to form and create a new bank so long as they meet the financial and regulatory requirements, and that they should not have to politically ingratiate themselves in order to achieve such legislative consent.

We do not think it is the responsibility of the legislator to exercise a judgment as to whether or not one group or another are more or less competent to operate a new bank. This is a judgment that should be reserved to the market place without overtones of what might otherwise require political influence.

5. We think the restriction against the ownership of non-resident banks operating in Canada is unwise and in the long term detracts from developing business maturity in the Canadian economy. It is reasonable to expect that Canadians within their own environment would have all the advantages of providing a service to their own countrymen. Instead of being afraid of having foreign banking operations in Canada, we should welcome them as a contributory element to broadening and expanding our foreign contacts, markets and communications. Canada is essentially an export nation. At the present time we have a major deficit in our international trade accounts and we are seeking to isolate ourselves from the very communications and facilities that would naturally expand this trade. To our knowledge most of the Western nations permit the operation of foreign banks, and for the Government to support a restrictive attitude towards the operation of foreign banks in Canada is a complete contradiction of the Government's purported policy of seeking to create a competitive environment in the banking system. Neither the Canadian banks nor the Canadian Government should have any fear from a foreign bank in our own domain if our system was capable of serving the consumer efficiently and competitively. If our present system is not capable of doing this, then we should rapidly correct the situation by allowing the progressive infiltration of a competitive system that would act as a preventative to our progressive atrophy towards becoming a backward nation.

6. We think Section 138 of Bill C-222 is completely out of perspective to the nature of this provision in the legislation. As we have pointed out in our original brief, and as is recognized by both the Government and the banks, the Canadian banks have during the past decade acted as one of the most highly organized cartels in our country.

This section of the new legislation proposes that if they continue in this manner they shall be fined \$5,000. With all due respect to those who drafted the legislation, this is ludicrous. The banks have literally acted as an avenue through which certain private interests have exploited millions of dollars of the Canadian public's money, and they are now being told that if this continues they will be fined \$5,000.

In the first case it is legislation that is very difficult and expensive to police. In the second case, if it is the Government's intention to dissolve this cartel arrangement, then it requires preventative legislation with a strong deterrent. The action is so contrary to the public interest that the minimum deterrent should be a very large fine plus prison penalties ranging up to five years for

those officers and directors of the bank who directly condoned or contributed with prior knowledge to the transgression of the law.

Lastly, we think the Canadian public have a reasonable right to understand the decisions made by the Government in the banking area. A large number of Canadians recognize that historically the concentration of banking assets is directly detrimental to the development of a competitive and free enterprise economy, and in the final analysis results in primarily serving a few private interests.

In view of this recognized principle, we think it is proper that the public should be advised and given an explanation as to the reasoning under which approval was given for the merger of the Canadian Bank of Commerce with the Imperial Bank of Canada. This action directly affected the lives and interests of literally hundreds of thousands of Canadians, and it becomes a matter of educational and public interest that Canadians should understand on what basis this merger was approved as being in the public interest.

Only through disclosures of this nature can the Canadian public be assured that the chartered banks and minority private interests do not exercise an undue influence on the Government of Canada for the pursuit of their own interests at the expense of the majority of Canadians whom the Canadian Government and chartered banks are committed to serve.

Appendix I

Sirs:

Having just read your brief to the Standing Committee on Finance, which certainly turns a spot light on the "combine" in the Canadian financial field, I cannot help but admire your courage.

Do you suppose if the brief is not noted and reviewed by the news media, it would be because of the tentacles of the combine?

Treasurer,  
A National Canadian  
Corporation.

Dear Sirs:

Thank you very much for your letter of October 8th, under which you sent me a copy of your brief.

I have only just scanned the brief but it does strike me as being what you refer to as a constructive approach to correcting the deficiencies of the Canadian banking system.

It had often occurred to me that the policy of accommodation rather than of competition was a weakness in our Canadian economy generally, and it is most heartening to find this thesis so cogently argued as you have done in your brief. I can only hope that the Parliamentary Committee will pay due attention to what you have had to say.

A Lawyer,  
Western Canada.

Sirs:

Your submission to the House of Commons is a masterpiece, and you are to be commended not only for its content, but also for your courage in making it.

A Lawyer,  
Montreal.

**LAFFERTY, HARWOOD & CO., MONTREAL**  
**BRIEF TO THE STANDING COMMITTEE**  
**OF THE HOUSE OF COMMONS**  
**IN OTTAWA**  
**ON FINANCE, TRADE AND ECONOMIC AFFAIRS**

August, 1965

*Subject:* Bill C-120, An Act respecting Banks and Banking—more commonly referred to as the Decennial Revision of the Bank Act.

We submit this brief in the belief that those who do not agree with the present system should so express their views.

We propose to discuss the Canadian banking system in this brief in very broad principles. Many of the thoughts themselves will be based on circumstantial evidence. We have not undertaken a documentary study, as a great deal has already been achieved in this field by the 1964 Royal Commission Report on Banking and Finance. Neither do we have access to various witnesses and documents that would be necessary if we were to present our views in the form of documented evidence. Our views, therefore, reflect only our own observations and exposure to the system over a collective period of some 15 years as participants in the financial community.

We are not critical of the conduct of those who manage and are employed in the system. They are, in our opinion, victims of the circumstances related to the defects of the system itself, and if they did not carry out their responsibilities as dictated by the present forces in play in the system, they would be replaced by those who would. The majority of those employed in the system are governed by economic circumstances. They have families and children, and although they may have convictions different from the actions that they are required to take, they are dominated by a system that requires their loyalty to the bank first.

For many years the view has been publicly expressed by Canadian bankers and other prominent persons that Canada has the finest banking system in the world. We suggest that, before the Committee accepts this view, they obtain the opinion of authoritative people in the Federal Reserve System of the United States and other prominent bankers in the United States, whether they agree with this viewpoint, and if so, why the U.S. has not adopted the same system in an economy that is broadly recognized as being the most efficient and productive in the Western World.

One of the secrets of the efficiency in the U.S. economic system is its highly competitive nature, whereby the producer of goods and services must cater to the demands and requirements of the consumer. This requires a greater vitality and output than the alternative system under which the producer decides the services and products that will be available to the consumer.



The vitality and entrepreneurship of U.S. industry and business can be directly related to the vigorous anti-combine and anti-trust legislation that is continuously being enforced in all areas of the economy. It is this action that provides the consumer with the widest range of choice and prevents those seeking to provide the goods and services of colluding in order to save themselves the efforts of initiative and innovation, and moving with the changing desires and needs of the consumer.

The Canadian banking system has developed into a nationwide, monolithic structure with the participants being governed by manuals and regulations designed to hold the system into a cohesive form that responds to a narrow management structure surrounded by interlocking directorates.

It is, in effect, a banking machine designed to respond to the policies of the hierarchy and not to the desires and choice of the consumer. Eventually, if these desires are registered strong enough, modifications permeate through the system, but it is a long reflective process.

Such a banking approach as this must seek uniformity in its policies, otherwise authority cannot be effectively exercised over such a vast network. The system thereby imposes conformity on the customer, irrespective of differences in regional areas and the different ideas that constantly motivate the millions of Canadians who use the banking system because there is no practicable alternative. The one exception is that the service accorded to a customer is graduated, depending on his importance to the bank in the overall scheme of things. Friends of the bank, that is to say friends of the hierarchy, receive special accommodation, special rates and special favours.

There are eight Canadian banks for a population of 19,500,000 people. In the United States there are 14,000 independent banks, catering to a population of approximately 190,000,000 people. In Canada, if we had the same proportion of independent banks in relation to the population, there would be 1,400 independent banks under independent management serving the country.

We will not propound the various arguments for and against the independent banking system and the branch banking system. They are numerous and it would lead to confusion in the theme that we have to present. In principle, however, the independent banking system has more incentive to develop regional growth and industry. More important, it protects the banking system of the nation from the influential control of small coalescing cliques.

As is well known, three of the Canadian Chartered Banks control 70 per cent of the assets of the Canadian chartered banking system. These three banks in turn directly or indirectly have, through their Board of Directors, effective influence and access to policies of the three largest Trust Companies in Canada. We made some calculations earlier this year that suggest these three Trust Companies either as custodians or managers, have in their orbit of influence something close to 50 per cent of the market value of all Canadian owned industrial stocks listed on the combined Toronto and Montreal Stock Exchanges.

Associated with each of the three largest banks, who in turn are associated with the three largest trust companies, are the three largest security underwriters in Canada. Underwriting in Canada is not on a competitive basis of bidding and price, as it is in the United States. Generally in Canada, it is on a basis of agreement and accommodation related to the influence each respective group can

exercise through its bank and trust company affiliation. It is in principle based on an agreed division of markets.

The entire banking structure itself, to be well understood, requires charting to show the interrelationship of banking directors to financial institutions, and from the financial institutions to the public and large private corporations, and then back to the chartered banks.

With all due respect, we suggest the Committee cannot judge the most suitable legislation for the chartered banks based on the broadest interest and welfare of the Canadian people and future generations to come, until these interwoven relationships have been documented and their significance is fully understood. Without such data, the observer may discern the skeletal formation of the system but he will never comprehend its motivating forces.

It is possible that the information could be compiled by an independent citizen or a firm such as ourselves. However, as some of it is not available to the public, we suggest that the responsibility rests with the Inspector General of Banks or the Department of Finance.

The last published statements of the three largest Canadian banks showed a total of 148 directors. Whether the number is adequate or not to direct the affairs of each bank to the maximum efficiency and interest of the majority of shareholders is a management responsibility.

However, when it is seen that 20 per cent of the directors of one of these banks are practicing lawyers, it starts to become evident that membership of a bank board is regarded not so much as a responsibility to the public as a potential opportunity for the leveraging of influence.

It is a well known fact that a practicing lawyer has neither the time, nor in most cases the knowledge or experience, to effectively judge and direct a nation-wide branch banking system that must necessarily relate to the international monetary and banking affairs of the world. It has connotations of the cement cartel dominated by lawyers, that until recently crisscrossed Canada.

Another Board showed that more than 70 per cent of the Directors were also Directors of Life Insurance companies. Again, this was not one Life company but several.

On one of the other Boards 50 per cent of the Directors were also Directors of Trust companies. Although this bank itself effectively controls one Trust company, many of these Directors were on the board of other Trust companies. This shows the range of cross pollination.

Many of the Trust companies themselves have regional advisory boards. For instance, one Trust company which has 37 directors has advisory boards across the country comprising 124 individuals, excluding directors also serving on the advisory board.

In this particular instance the Chairman of one of the advisory boards of this Trust company serves as a director of the bank that controls its major competitor. As such, he is in the role of listener and interpreter to both sides. It is quite obvious that in a truly competitive spirit of enterprise he could not serve both organizations loyally or to the full measure of his ability.

Perhaps the outstanding example of this inbreeding is one of the leading life companies. It is now mutualized and has thereby lost its own initiative and vitality.

In this particular case the Chairman of the Board is among the most experienced and prominent directors of the largest Canadian bank.

Sitting on the board under his jurisdiction is the Chairman and Chief Executive Officer of the second largest bank. With him on the same board is a prominent director of the third largest bank, and also the Chairman and Chief Executive Officer of the fifth largest Canadian bank. The Life company in question holds in its portfolio 20% of one of the three largest Trust companies, which is an important minority position in the 'chess game' of power that is played in this field.

In terms of evolution and human relations these patterns are understandable because there is no legislation which says it shall not be so; but in terms of the public welfare and interests of the Canadian people, it represents the domination and exercise of power for the interests of a few.

None of these directors can be loyal to their own customers and shareholders and loyal to their competitors at the same time. We do not question the motivation of many of them. Many of them believe they are protecting the shareholders' interest from less desirable influences and in this capacity they are therefore serving their respective companies. In truth of course they are not. It is a false protection. The real such protection should stem from operating management whose efficiencies are such that their position would be impaired if less desirable elements sought to exploit the assets. Then the directors could and should appeal to the shareholders for support, showing that otherwise the value and earning power of their assets would be damaged. It is then up to the shareholders to exercise their own independent judgment.

As it is, under the present system the operating management has so many masters with policies of accommodation, all it can do is bend with the wind and hope to ingratiate itself. It has no motivation of its own and cannot have under this system. If it did it would challenge the fabric of the structure and such motivations would be suppressed or the originating force would be chastised as a troublemaker and deprived of authority. If an individual did not mend his ways he would probably find himself transferred to some isolated spot to complete the rest of his banking career.

Thus are Canadian corporations deprived of good operating management in depth. Those with talent either remain frustrated on the sidelines awaiting new opportunities, or migrate to the United States, where entrepreneur qualities and ability commands a premium price because of its economic value in the affairs of finance and trade. The end consequences of these characteristics to the customer and the economy as a whole are self-evident. It results in a banking system without integrity of principle or initiative of its own.

As a matter of interest, the following are the published directorates of the President and Chief Executive Officer of one of the three largest banks. There are some other directorates known to be held that are not included in this published list. It is quite obvious that under these circumstances this officer cannot be devoting his full energies to his bank, which on the basis of his compensation the shareholders have a right to expect.

President and Chief Executive Officer of:  
one of Canada's three largest banks.

Deputy Chairman—Bank of London & Montreal Ltd.



## Directors of:

The Ogilvie Flour Mills Co. Ltd  
Canadian Pacific Railway Co.  
The Consolidated Mining & Smelting  
Company of Canada Ltd.

## Director of:

Consolidated Paper Corp. Ltd.  
The Steel Co. of Canada Ltd.  
Canadian Cannery Ltd.  
Sun Life Assurance Company of Canada  
Canadian Investment Fund Ltd.  
Canadian Fund Inc.  
The International Nickel Co. of  
Canada Ltd.  
United States Rubber Co.  
Western/British American Assurance  
Companies  
The Montreal Boy's Association  
The Seigneurie Club Community Association Ltd.  
Canadian Council, International  
Chamber of Commerce.

## Member of Investment Committee:

The Canada Council  
National Industrial Conference Board  
The Royal Empire Society (Montreal Branch)  
Canadian General Council The Boy  
Scouts of Canada

## Member of Metropolitan Board of Directors

Y.M.C.A. (Montreal)

Member National Board of Directors—Canadian  
Cancer Society

## Member Advisory Board:

Royal London & Lancashire  
Rehabilitation Institute of Montreal  
Dollar Sterling Trade Council

## Member Board of Governors:

United Red Feather Services  
Canadian Export Association

## Member Board of Trustees:

The Newcomen Society in North America  
(Chairman)  
The Red Cross Society (Quebec Prov. Div)  
Health League of Canada (Member Board  
of Honorary Advisory Directors)

Governor of:

Royal Victoria Hospital (Member of  
Finance and Executive Committees)  
Sir George Williams University

Miscellaneous:

Boy Scouts of Canada (Honorary Vice-  
President—Montreal Region)  
St. John Ambulance (Honorary Director—  
Quebec Council)

This is not creative banking. This is the use of the machinery for the exercise of power. To the individual there may be benefits, but it is the bank and shareholders who consequently suffer. The principle of the legislation now being considered is to formulate a banking system that will truly satisfy the requirements of our country.

What does the present system mean in terms of economic efficiencies, and does it really serve the shareholders' interests? It means different things in different areas. In the grass roots level of the banking system it means that the Branch Manager in a certain geographical area is governed by the policies of a Board of Directors who are looking at matters in terms of accommodating each other. If the interests of the regional area should happen not to coincide with these policies of accommodation, then it is the regional area that suffers.

What does it mean in terms of personnel? It means that in a banking system that has 5,650 branches, the operating personnel must conform. The system thereby suppresses initiative, change and new ideas because these challenge the authority of the system. The customer must also conform, even though his needs may be different, because a deviation from the manuals and regulations would again challenge the authority of the system.

It means that a system is created that is wide open to abuse and exploitation by a few strong individuals. By forming small cliques serving on different bank boards, those at the apex of the pyramids are in a position to acquire and exchange information that would not otherwise be available. This is the nucleus of men who dominate the Canadian capital markets, and who by the creation of investment trusts are further able to exercise their power throughout Canadian corporate life.

There are many historical examples of good medium and small companies that had real growth prospects which have been swallowed up. They had no alternative because they had no protection from price cartelization. Good and growing management must then surrender to the dictates of larger interests or be lost. Industry becomes concentrated, immobile and resistant to technological and marketing changes. The consumer ultimately suffers and more efficient U.S. industry invades the Canadian market place, and a serious imbalance in our trade figures result. Under these conditions secondary industry, which is so important to the future industrial development of Canada, cannot thrive. It is the exercise of power by a few that is motivated not by efficiency, but by personal benefits.

It is false to argue that abuses are the exception rather than the rule. A documentation of records would show that much of the major personal wealth in Canada has been acquired in this manner.

It is a system that provides greater opportunities for the less scrupulous than those of integrity, because he who seeks to preserve and protect the interests of the customer challenges the authority of the system.

In industry it leads to a system which restricts and prevents the formation and development of new competitive elements. An examination of the three largest banks will show that in most instances each has a dominant orbit of influence in the major industries of Canada. If, for example, a group in Winnipeg decided for one reason or another they would like to finance and develop a steel mill, they would very soon find that their plans were no longer confidential, that they could not get support in the capital markets, and that many of their potential customers were coming under threats of economic intimidation.

What does it mean in the Canadian capital markets? It means that those institutions which by the nature of their business have a continuous flow of savings, are subject to the collusion of the investment underwriters who, on their own terms, distribute new and previously outstanding securities.

It means that all others in the financial capital markets must ingratiate themselves, and in many instances compromise the position of their investor clients, in order to be allowed to make a living in a system where they cannot compete by energy, talent, initiative or greater efficiency.

It is a system of graces and favours where the consumer is given what he can get, and in many instances must prostitute himself for that which he receives. It means that honest men must perjure themselves to sell securities in which they do not believe because they too have economic problems of subsistence. It means financial analysts must write slanted reports on certain situations if they are to retain their jobs. It results in manipulated price markets, and extensive abuses throughout the stock exchanges in Canada at the expense of the Canadian investor.

These Exchanges are under provincial jurisdiction, but the provincial authorities cannot organize to correct the wide-spread malfeasance that pervades these markets when the dominant influence that has created these conditions is under Federal jurisdiction. The provincial governments themselves are not free agents in raising their capital requirements, because the capital markets are dominated by a single structure, and if the governments of the provinces require funds, they are beholden to this group for accommodation. In effect, therefore, this group is in a position to exercise an undue influence on the provincial government authorities at the expense of other Canadians.

What does it mean in Corporate management structure? It means that the large Canadian corporations have a Board that is dominated by these influences, and the Chief Executive Officer is in the position of having to conform in his corporate policies. He may find that his markets are defined for him, and also his source of raw materials, and whom he may or may not employ. This in turn means that the majority of Canadian public corporations, unless they are controlled by U.S. parent companies, are instead of being orientated to serving the consumer to the best of their ability, are required to respond to influences that may have nothing to do with their direct business. As a result, younger Canadian



management talent finds that its own initiative and energy is suppressed because it would otherwise antagonize this orientation. Operating policies become based on expediency; not on principles and corporate objectives designed to serve the consumer by initiative and new ideas.

As a result, it means that the learning institutions of Canada are required to teach at a level of mediocrity in business administration, finance and economic affairs. Many of their endowments and those sitting on their Governing Boards interrelate to the directorates of the Canadian Chartered Banks, and were they to aspire to teach differently, they too would be challenging the influence of authority on the hierarchy structure.

The financial press in Canada, which is highly concentrated, is equally required to play its part and reflect the views of the dominant interests. Controversial or unfavourable news is published only when extreme pressures require, except or unless it does not directly affect the dominant interests. Then it is expanded out of all proportion to its importance. The press is conditioned by pressures that exercise an influence on its advertising revenue. As a result, the Canadian investor is often denied proper and vital information. The Chartered Banks and the financial underwriters are particularly influential in slanting news copy.

It is an insidious system that creates a class structure and milks the majority for the benefit of a few. The results, besides the sociological and political aspects, are that as the Canadian corporations are denuded of talent and ability, they can no longer vigorously meet the competition of U.S. corporations which are conditioned by the disciplines of having to serve the consumer. Most Canadian corporations lack vitality and talent in depth. As a result, it is frequently seen that when the leading personality of a Canadian corporation retires or dies, the assets have to be sold to a non-resident, otherwise substantial losses would result because the structure itself lacks the management depth to continue to compete effectively.

It means in broad principle that inside information is available to some in capital markets that is not available to others. The price structure of these markets therefore becomes distorted by this pervasive influence, and these markets are no longer free, responding to the influences and conditions in the economy. It also means that the average Canadian investor cannot move in those markets freely without fear of exploitation, and under such conditions he does not participate. As a result, the Canadian public ownership in the shares of Canadian industry and production is probably less than one-third on a prorata basis than that of the United States.

When the capital markets are not properly regulated and are subject to continuous exploitation and abuse, the natural and correct flow of savings does not materialize. The New York markets, by contrast, are the most highly regulated in the world. It is this regulation that allows the tributaries to flow freely in without fear of abuse. The net result in Canada is that much of our savings are stagnant, or sterilized into positions and areas that are neither creative nor productive. As a consequence, to develop our growth and expansion we have to continuously borrow in the markets of New York and elsewhere, and progressively in the last 20 years we have been selling our assets in order to maintain and support a monolithic structure that is influenced and dominated by a small group of interests.

In effect, it is a banking system which has developed into the creation of feudal commercial empires. The permeation extends down to the legal and audit firms who feed off the central system.

These empires, in medieval fashion, have their own castles and compete to see who can exercise the most power and build the biggest head office.

In the long term the sociological impact is on the character of the country as a whole. We are no longer a people of self-reliance and independence. We are a kept people, dominated by the policies of the U.S. because we are now financially indebted to them, despite our tremendous resources and natural wealth.

Perhaps the fickleness of the Canadian banking system is best reflected in the services that are offered potential U.S. customers and those offered Canadians. This shows quite clearly in Canadian bank advertising.

The following pages contain some recent Canadian bank advertisements cut from the New York Times, the Wall Street Journal and the American Banker.\*

The first page shows Canadian banks boasting that they can blaze business trails anywhere in Canada and help prospective U.S. customers find the "big ones".

Another advertisement offers to open executive doors across Canada to any prospective U.S. customer. In neither of these two instances are the same offers made to Canadian prospective customers. These advertisements are not run in Canada.

It will be seen in the U.S. advertising that great emphasis is placed on the information available to the prospective U.S. customer from the national branch system in Canada.

This same offer is not made to Canadians, although it is their information that the banks are gratuitously using as bait to attract prospective competitors from the U.S.

We do not think the majority of Canadians would approve of these policies and conduct on the part of the Canadian banks if they were aware of them. It is, in our opinion, a direct betrayal of trust and confidence.

The last page shows the type of advertising the Canadian banks offer in Canada. It is bland, institutional advertising, talking in vague terms of convenience, but with nothing specific. This type of advertising combined with a few flashing neon signs and some billboard 'sloganeering' is the treatment designed for the Canadian.

The Canadian advertising of one bank proclaims that its staff is, in some undefined way, superior.

This is hypocritical. It is a fact that the Canadian banks have a compact under which (with some rare exceptions), they will not hire from another bank. This is contrary to the practice in either the U.S. or Europe, and essentially means that if a bank employee is dissatisfied he cannot normally expect to receive employment consideration from another Canadian bank.

This is one of the policies used to regiment the system. However, the point to be made is that if a bank is not willing to hire better talent away from another bank, then it is self-evident that its claim to superior staff is without foundation.

\*The advertisements referred to are not included in these Minutes of Proceedings and Evidence.

It is interesting to pause and speculate what motives prompt this divergence of advertising policy.

The prospective U.S. customer is offered all sorts of services—particularly ones giving access to information.

The banks are, in effect, selling the knowledge acquired by them through having conducted business for their Canadian customers. The three largest Canadian banks do not have investment or economic research departments of any consequence. They have never fostered this development because such a growth within the bank structure itself would challenge the authority and power of the interests of the interlocking director structure. Most of the financial and business knowledge is gained by their contacts through their numerous private channels of communication among the group interests. Also, cheques passing through the system are another source of information.

It is a known policy that the Canadian banks will not give investment advice to the Canadian. They will instead send the enquirer along or put him in touch with one of the brokers or investment dealers within their sphere of influence.

The Canadian banks know very well that they could not run the advertisements that they run in the U.S. press in newspapers in Canada, because immediately they started to receive enquiries for services that they were offering, they would be suppressed by the dominant interests who, to maintain their structure, seek a status quo rather than a competitive environment.

It is for this same reasoning that the Jews in Canada have been largely excluded by direct restrictive practices from entering the financial community. There are no Jewish member houses of the Montreal Stock Exchange, and the last such applicant was blackballed by the Members of the Exchange. There is now one Jewish member firm in Toronto. This compares with the large and broad participation of the Jewish community in New York, London and Paris, and all the developed financial centres of the Western World. It is not a question that the Jewish community have neither the ability nor the desire to enter the business. It is a restrictive measure based on fear of competition that would disturb the structure and status quo of the dominant interests.

Before closing this Brief with our recommendations, there are two thoughts we would like to leave with the Committee. The first of these thoughts is best expressed in the quotations of two men, both with different political backgrounds.

The first of these is a quotation from Senator Estes Kefauver, who in his book titled "In a Few Hands: Monopoly Power in America", stated the following:

"High prices are a direct, immediate, and easily recognizable consequence of monopoly. There are other consequences, equally costly but less obvious in their impact. They arise from the kind of competitive practices which come into being when price competition is ruled out of the industry. Whenever there is more than one firm in a business, some form of rivalry is inevitable; if price competition is barred, this competitive behavior will take other forms.

"But so long as it is competitive activity, what's the harm? The fact is that non-price forms of competition yield very different results from those flowing out of price competition. These results involve great economic waste and are often positively harmful to the economy."



The second quotation comes from the Memoirs of Herbert Hoover, who gave nine reasons for the causes of the Great Depression in the United States in the period of 1929 and onwards. (The U.S. banking system was reformed subsequent to this debacle, and included very strong preventatives against interlocking interests and directorates.)

"Nor was our financial weakness solely in the banks. Throughout the whole business of providing capital for our economic life there ran a pollution—the habit of making money by manipulation and promotion of securities. And that promotion too often disregarded the merits of the goods it sold. In addition, the financial world, instead of providing merely the lubricants of commerce and industry, had often set itself up to milk the system. Worse still, instead of being financial advisers to commerce and industry, the financiers had, in many cases, set themselves up to dictate the management of it."

The second thought we should like to leave with the Committee is very straight forward. The Federal Parliament has the full responsibility and authority for banking in Canada. Those who have been elected to carry out this responsibility represent the Canadian people as a whole, and not the minority interests of power and influence. If the Federal Parliament fails to provide legislation that will eliminate the abuses and dominant monopolies that have crept into the system, the people of Canada will place their trust in those governments at a lower level that will respond by administering and protecting their interests.

The entire challenge to future confederation is based on the support that the Canadian people will give to those in elective office. If these in turn will not respond where they have the power and authority to do so, the electorate will transfer their power to others who will respond. If the Federal Government fails in this area, the Provincial authorities will be under strong pressure from the electorate to provide them with proper and equitable protection from the abuses, pressures and influences of small private pressure groups seeking to expand their interests at the expense of the majority of the population.

On the following pages we have briefly outlined in principle those changes that we think should be incorporated in the proposed legislation. We have not attempted to draft these or designate the section of the Act in which the various principles should be incorporated in the proposed legislation. They are sufficient in their form to reflect our views.

The Act as submitted to the Committee reflects the Government's proposals. In our opinion it pays only lip service to the conditions that exist. That which we have broadly outlined in this brief can be easily substantiated and much of it is available in documented form in the Porter Commission Report.

We believe we have expressed our views in a fairly comprehensible and straight forward manner in this brief. We do not therefore think it is necessary for us to appear in person before the Committee. We would, however, be glad to do so in confrontation with a spokesman of any of the Canadian Chartered Banks if they should seriously wish to challenge any of the viewpoints we have expressed.

## RECOMMENDATIONS

The intent of these Recommendations is that all Directors serving on the Boards of Chartered Banks would be in a position whereby their decisions were of an arms length nature without conflicting interests so that their services were primarily in the interests of the majority of the shareholders and not for private interests.

## SECTION 19

*Proposal*

A director shall not be eligible to serve as a director of a bank if he is already a director of another financial institution. A financial institution to be defined as a trust company, life insurance company, caisse populaire, an open or closed-end investment company or other repository of public savings.

*Purpose*

In banking and finance two masters cannot be reliably served at the same time. There are conflicting interests involved. The shareholder has the right of undivided interest from the directors of his bank.

Against the argument that other institutional relations give the directors more breadth and experience, the counter argument is that management should develop its own research and economic departments and develop operating self-reliance from within the bank organization.

*Proposal*

No shareholder shall serve as a director if he is also a member of the House of Commons or the Senate in Ottawa, or an elected member of a Provincial legislature.

*Purpose*

Dual positions of this nature lead to conflicts of interest and the peddling of influence and power by those who have been elected to serve the people.

With respect to members of the Senate, they are all adequately paid and to use a public position to further private interests is an abuse of public confidence and position.

*Proposal*

No Officer of a Canadian Chartered Bank shall serve as a director of any corporation, whether resident or non-resident in Canada, so long as he is an officer of the bank.

*Purpose*

The officers of the banks are adequately compensated. Their time should be devoted exclusively to the interests of their bank customers and shareholders. Some Chief Executive Officers of banks hold as many as 20 to 30 outside directorates. They are thereby using the confidential information that accrues to them to further their own interests. It is an abuse of trust and confidence and also introduces a conflict of interest. To argue that it maintains customers for the bank by having representation on the Board is not valid. Customers should be attracted and maintained by the efficiency of the service and price benefits, and not by underhand inducements.

*Proposal*

That the annual proxy to shareholders shall list those directors that it is proposed to nominate in the ensuing year. This proxy will disclose all outside directorates already held by the nominee and also the number of shares of the bank held by each.

*Purpose*

This is normal and reasonable information that a shareholder should have before making a judgment as to how he should execute his proxy.

*Proposal*

That all directors and officers of the Chartered Banks should report in the annual proxy all transactions they have made individually in buying and selling the shares of the bank, showing amounts and the date transacted.

*Purpose*

This is in accordance with the new Canada Corporations Act 1965, which does not govern the banks. It is proper and correct procedure to prevent inside trading abuses.

*Proposal*

That the Chartered Banks should be required to report to their shareholders quarterly, with an income statement as per Schedule "Q". The Government legislation proposes once a year.

*Purposes*

1. It imposes an operating discipline on management and makes them more responsible to the shareholders.
2. Through the public ventilation of figures, promotional activities on the Exchanges are reduced.
3. It is now accepted universally as a proper and responsible practice to report quarterly to shareholders. All the major banks in the United States do.

## SECTION 76

*Proposal*

A Bank shall not hold the shares of any corporate stock except a corporation owning premises used by the bank.

*Purpose*

The Government legislation allows for a 10% holding. We think the banks are in the banking business and this is where they should stay. Any outside activity is in potential conflict with their customers. A bank holding 10% of a corporation either with friends, or in association with another financial institution is in a position in the Canadian market to exercise an undue influence on that corporation.

For portfolio purposes we do not think corporate stocks should be held. The business of banking is lending, not speculating in common stocks.

*Proposal*

There should be no interest rate ceiling that the banks may charge.



*Purpose*

It is not the function of Government legislation to dictate the terms under which the entrepreneur in a free economy will conduct his business unless that business has a monopoly position, in which case the consumer should be protected.

We are opposed in principle to the arbitrary fixing of an interest rate ceiling by a process of legislation. Rates and prices are matters that should be governed by open market conditions. It is the responsibility of Government and legislation to see that those markets are properly regulated, free from fear and intimidation, and equally accessible to all participants without regard to creed or class to participate if they should so wish. It is Government's function to see that the consumer is not exploited by cartels and agreements of collusion. The proper dissemination of information is essential in this process so that prices and rates quickly respond to the demands and wishes of the consumer. If legislation achieves these conditions effectively, no other intervention is necessary. The consumer will migrate to the efficient at the expense of the inefficient. It is not Government's role to dictate or organize the consumer. If left with freedom of action, he is perfectly capable of looking after himself.

The Act should embody the following:

1. The Act should clearly define "interest". This would rectify the present situation in which part of the cost of borrowing money is sometimes described as a service charge.
2. The Bank of Canada should take over the operations of clearing cheques for all banks, so that ready access to the Canadian banking system is available to eligible participants.
3. Membership of any officer or director in any association providing the facilities for collusion should be prohibited.

## APPENDIX "EE"

Gentlemen:

Canadians per capita have only about  $\frac{1}{2}$  as much of their savings in common stocks as Americans have, yet we squirrel away much more than they in savings accounts and insurance. It is no wonder that our industries are over 50 per cent foreign owned; some, (autos) 90 per cent. I feel, as do others more knowledgeable than I, that the main reason is that we simply do not trust our stocks or stock markets.

Dr. Morton Shulman, Toronto's genial chief coroner who is said to be equally at home cutting coupons or cadavers, recommends the following in his recently published book: "The fact is that one is better advised to buy U. S. securities"... "One reason that stocks in Canada remain at bargain prices is the erosion of public confidence"... "With the greatest regret I must say that 'Buy Canadian' is a great formula everywhere except in the stock market. There are exceptions where stocks are vastly underpriced, but except for these uncommon securities, it is better to avoid Canadian stocks. It is with difficulty that I as a Canadian must recommend, other factors being esqual, 'Buy American'."

Professor C. A. Ashley, of the Department of Political Economy, University of Toronto, put it this way in his scholarly brief before the committee studying company law at Queen's Park, "It is somewhat humiliating that the only companies operating in Canada that make adequate disclosure are those whose shares are listed on the New York Stock Exchange".

Our financial editors have been writing about the problems of corporate disclosure and shareholders rights for years; the thoughtful articles and editorials reproduced at the back of this brief are representative of their feelings.

It is heartening to note that there are signs that things are changing for the better, brought on in no small measure by the Atlantic Acceptance-British Mortgage farce. Here in Ontario the select Committee on Company Law and the Attorney General's Committee on Securities Legislation are both recommending wide-ranging changes in securities laws, giving more information and protection to the investors; likewise the revised Canada Corporations Act.

Even the Toronto Stock Exchange which our American friends regard as little better than a gambling den with the dice well loaded in the house's favour, is tightening things a little after the Windfall Mines debacle.

You gentlemen on the Bank Act Committee have the opportunity to strike a real blow for shareholders democracy, for the banks have by far been the worst offenders in the field of corporate disclosure. This is ironic, because as anyone knows who has ever applied for a bank loan (and who hasn't) they quite rightly insist that the borrower bare his financial soul. Should our bankers do less to their shareholders and employers? After all, what have they to hide?

A further thought I would like to put before you gentlemen is this: Think of the power which rests in the hands of banking's top management, with very few democratic checks and balances. It is largely conceded that our banks' boards of directors, distinguished and knowledgeable business statesmen though they doubtless are, are largely decorative. Most are either large depositors or borrowers, and too busy at their own affairs to pay much attention to the bank. Many are directors of so many firms that they couldn't possibly have the time to do an

adequate job of guiding the banks' affairs. Which leaves this awesome economic power in the hands of the very few in top management. Doubtless these gentlemen, most of whom have worked their way up through the ranks over many years, use this power for the good of the country and of their shareholders. Why then should they be so reticent?

Professor J. E. Smyth of the University of Toronto expressed his quiet concern before the Select Committee on Company Law in Ontario as follows: "This brief is not intended simply as a plea for the recognition of shareholder rights from the point of view of the shareholders themselves, for all such a position might be justified. I submit that one of the ways in which we can avoid an oppressive concentration of power in modern society is to maintain the kind of groups that act as a check on one another".

"A system that requires management to be accountable in some reasonable degree to shareholders also keeps management accountable to society as a whole; shareholders, in fact, act on behalf of society".

As things are now, bank profits are managed by moving money around in the various reserve and rest accounts, so as to give a pleasant and complacent picture to the shareholders and depositors. All bank stocks move within the same price-to-yield range, so there is no way to gauge the efficiency of the various managements. It would appear that our bankers are nowhere near as efficient as their U. S. Counterparts. For example, U. S. banks manage to get a 10-12% return on average on invested capital; the best we can do is 8% or less. It is generally thought that bank employees are not overly well paid; as a matter of fact several of our banks went cap-in-hand to the Department of Labour a couple of years ago, asking to be excused from paying the minimum wage, presumably because they couldn't afford it. It would therefore appear that either top management are paying themselves too well, or more likely that personnel are not deployed in the most efficient way, because in Canada salary over-head is as high as 1.50% of total assets while in the U.S. comparable banks are in the .74 to 1.05% range. There is also strong evidence that our branches are over-expanded; one report says that nearly  $\frac{1}{2}$  of the Toronto branches of one bank are losing money.

Certainly one wonders if we really need a bank on every second corner, as it often appears. We have one bank for each 3,500 people, as compared to the U. S. figure of one for each 5,500.

In the U. S., under the Securities Acts Amendments of 1964, banks, it has been decided, have essentially the same responsibility to their shareholders as other corporations, and the new act ends their blanket exemption from the coverage of the securities acts of 1933 and 1934. Many U. S. Bankers fought the amendment tooth and nail; however they now accept it, see the speech of the President of the American Bankers Association and what's more seem to be thriving on it. Compare for example the actions of the Management of the First National City Bank which found itself in an embarrassing spot of discovering a huge loss during a stock offering, and disclosing it even though it might have



jeopardized the sale—with that of our Canadian Banks which were caught to the tune of millions in the Atlantic Acceptance fiasco, yet made no mention of it in their financial reports.

Very seldom does one find a Canadian Bank's president, when reading his speech at the annual meeting, discuss anything but the state of the economy in general terms. Pick up any of our banks annual reports at random. Do you find it as informative as that of the Moscow Narodny Bank in London? This institution is wholly owned by the Russian Government.

This report being too long to photo-copy, I have sent one to the Secretary of the Committee.

To aggravate matters further, secrecy seems to spread over companies with which the banks have close dealings. An example of this is Gunnar Mines-McNamara Construction, companies which have recently fallen upon evil days. A consortium of banks are said to be now running these firms to get their money out (the figure was reported to be \$45,000,000.00). Shareholders of the Gunnar group naturally wanted to know what was going on, but management couldn't tell them because "Their bankers disapproved".

I respectfully submit the following recommendations for your consideration:

1. Annual returns should be in every respect complete. Even the most knowledgeable of analysts at present find them virtually meaningless. Loss experience, specific reserves, contingency reserves, and tax-free inner reserves should be disclosed as well as those after tax. The sum total of reserves put away over the years should also be disclosed, as this is lendable capital. What is more, the statement should be set up in such a way that an average investor can understand it. (See the article by Vince Egan, showing the absurd lengths one must go to in order to make any kind of a meaningful comparison.)

2. Cumulative voting should be made mandatory in order that small shareholders can have a voice on the board of directors. (This was recently recommended by Ontario's Select Committee on Company Law, and is the law in the U.S., under the National Bank Act.)

3. Brokers should be forbidden from voting stock which belongs to clients but which they hold in street name, but should be obliged to pass along proxies to the beneficial owners.

4. Proposals which are to be put before the annual meeting by management, should be included with the proxy solicitation material, so that an owner who cannot attend the meeting can express his approval or otherwise. (This will soon be the corporation law in Ontario.)

5. Management should be obliged to send resolutions which are to be presented by independent owners at the annual meeting, along with their own proxy solicitation material.

6. The names, addresses and holdings of every shareholder should be available to any other shareholder at the bank's head office or at any of its transfer offices.

(Under the present system, one has to go to Ottawa in order to look at a shareholders list. Even then only holders of 500 or more shares are listed, and this list is generally a year or so old at the time of the annual meeting, or at least

this was my experience. Holders of 500 or more shares are less than 10 per cent of all shareholders. The latest figures from the Finance Department are:

October, 1965	Total Shareholders	Under 500	500- 1000	Over 1000
Montreal .....	24,099	22,544	845	710
Nova Scotia .....	14,063	13,112	498	453
Toronto-Dominion .....	14,428	13,505	468	455
Provincial Bank of Canada .....	5,433	5,095	201	137
Canadian Imp. Bank of Commerce .....	28,117	26,269	1028	820
Royal Bank of Canada..	26,724	25,038	907	784
Canadienne Nationale ..	5,528	5,069	251	208

This patently unfair arrangement effectively frustrates small owners from communicating with each other.

7. The Inspector of Banks should be empowered to find out who are the beneficial owners of bank shares in banks' nominee names, and the information should be made available to the public. (There are tens of thousands of shares registered in names like "Bankmont & Co.", "Gee & Co.", "Roycan", "Montor", "Lake & Co.", etc., which are known in the trade to be nominees for our banks. Banks are prohibited from owning their own shares, yet in the present Act there is no public official empowered to enforce this provision.)

8. Included in the annual return should be the amount of loans on which no payment on principal or interest has been received for six months. (If there has been a substantial loss, the owners should know about it. The argument that disclosure of large losses would be bad for public confidence is nonsense. As it is, owners have almost no way of judging their management's performance.)

9. The Inspector of Banks should be required to supervise closely loans made by banks to finance companies. (So much has been written of late about Atlantic Acceptance—British Mortgage, that I could hardly add anything to it. Apparently the situation was so bad shortly after the collapse, that unless the Bank of Canada had stepped in and arranged that huge amounts of cash be shovelled into many finance companies, the whole house of cards would have fallen in. The Controller of the currency in the U.S. feels the situation is serious enough there to warrant tighter supervision following the failure of Pioneer Finance in Detroit. This firm it would appear is in trouble largely due to the enterprises of the well-known Texas bon-vivant, Billy Sol Estes, now a resident of Leavenworth, Kansas.

10. Shareholders should receive reports quarterly.

11. Salaries should be disclosed of officers of the rank of Regional General Managers and up. Also information as to stock options and pensions.

12. Any inside trading of stocks by officers or directors should be disclosed to the Minister within 30 days of the transaction; to be published in the *Canada*

Gazette. (This is now mandatory for any company whose shares are listed on the London Stock Exchange, an institution particularly forward-looking.)

13. Directors should be limited to the number of boards on which they can serve—5 at the most. (Many are now on 10 or 15 and couldn't possibly pay enough attention to the complicated affairs of the Bank.)

14. An owner should be able to change his proxy up to the time of the actual vote.

15. Proxies should have a blank space on them so that an owner can fill in the name of a person to represent him at the annual meeting other than management.

16. Annual reports should be in both French and English.

17. The Governor of the Bank of Canada should be consulted prior to any proposed merger or amalgamation, to determine if it is the public interest. (When the Commerce and Imperial Banks merged, the 16th largest bank in the world was created, with assets of \$6,208,405,418.00. The merger, no doubt, made good business sense for the shareholders concerned, but competition in the Banking Industry in Canada was substantially lessened. And as Graham Towers is quoted as saying a few years ago when our bankers were opposing the entrance of the Mercantile into the business on the grounds that we already had too many banks, "It isn't exactly like the ladies ready-to-wear business yet".)

The American Bankers Association asked a group of U.S. bank stock analysts what information they thought should be included in an ideal bank financial report. Thanks to Harry V. Keefe, Jr. of Keefe, Broyette & Woods Inc., this information is appended. See also his article "The Case for Disclosure" as it appeared in "Bankers Monthly".

Good Luck To You All

Terry Howes

Erindale, Ontario.

*Editor's note:* Articles and newspaper clippings appended to Mr. Howes' original brief are not reproduced in this Appendix.















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